

VLT GAMING IN CANADA

PREPARED FOR:



PREPARED BY:



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Foreword by Canadian Gaming Association

A Clear Picture

This Study, *VLT Gaming in Canada*, is the first of a series of science and fact-based national studies and surveys relating to Canada's gaming industry that the Canadian Gaming Association (CGA) will be commissioning.

The Association commissioned this Study to provide a clear, comprehensive picture of VLT gaming across the country. This includes the motivation for initiating regulated VLT gaming, the evolution of the programs in each province, as well as current status and trends. Although not a study or analysis of responsible gaming, the study includes a compilation of the responsible gaming programs and policies undertaken by governmental agencies.

Well-Regulated, Accountable, a Major Contributor

Among the findings of the Study are that VLT gaming in Canada: is well regulated and operated honestly and with a high degree of public accountability by Crown agencies; offers entertaining, fair games in safe, age and access-controlled environments; raises significant non-tax revenues to fund key government programs and initiatives; and that Canada is at the forefront of responsible gaming program initiatives.

The Study shows that, since its inception, VLT gaming has returned almost \$20 billion to provincial government programs and services across the country. The Study also notes that Canadian provinces currently spend a total of \$75 million annually in funding for problem and responsible gambling programs – more than any other jurisdiction in the world.

It also contributes a great deal to people and businesses in communities across the country.

Fulfilling a Mandate

The Study is a key step forward in the Association's mandate to create a better understanding of the gaming industry by bringing facts to the general public, elected officials, key decision makers and the media through education and advocacy. Since formation, the Association has established relationships with industry participants and stakeholders on multiple issues – including responsible gaming policies and practices.

The Industry's Obligation

The gaming industry has an obligation to provide safe and secure venues and to assist those individuals who may be playing beyond their limits. This is not an easy or straightforward undertaking – to help individuals address their own personal dependence challenges.

Prevention, research and treatment are essential to combat all forms of self-destructive behavior. The gaming industry takes a leading role in this. In Canada, government agencies spend millions of dollars annually on problem gambling prevention; research and treatment, including public information programs to assist individuals make informed choices. Again, Canada spends more annually in this regard than any other jurisdiction in the world.

The Canadian Gaming Association supports the *Reno Model*, a science-based framework for responsible gaming, developed by Alex Blaszczynski (University of Sydney & Westmead Hospital, Australia), Robert Ladouceur (University of Laval, Quebec) and Howard Shaffer (Harvard Medical School, Boston).

Reno Model findings and recommendations include:

- *The majority of the adult population gambles responsibly.*
- *Only a small minority of the population develops gambling-related harm.*
- *Any responsible gambling program rests upon two fundamental principles:*
 - *The ultimate decision to gamble resides with the individual and represents a choice, and*
 - *To properly make this decision, individuals must have the opportunity to be informed.*
- *Within the context of civil liberties, external organizations cannot remove an individual's right to make decisions.*
- *In addition to viewing gambling as a choice, responsible gambling also rests on the principle of informed choice.*
- *Informed choice should be based on providing relevant, empirically-based information to help the players to make their decision.*

To quote Dr. Shaffer, the Director of the Division of Addictions at Harvard Medical School:

“There is a myth regarding addictive behaviors around gambling, that the game causes the disorder. In fact, the game doesn’t cause the disorder, because if it did, everyone who played the game would end up with the problem. It’s the relationship of a person with vulnerabilities to the games that they play, what this means to them and how it fits in their life, that essentially determines whether or not they will have a problem.”

The work undertaken by such experts can help readers of this Study understand and assess measures undertaken in Canada.

A World Leader

The Canadian gaming industry is at the forefront of responsible gaming programs. Based on the most recent Canadian Gambling Digest, Canadian provinces currently spend approximately \$75 million on problem gaming treatment, research, awareness prevention initiatives and responsible gaming programs.

Specific to VLT gaming, all provinces offering this form of gaming have developed and implemented responsible gaming programs that include both general messages and specific features installed on the VLT terminals themselves. Improvements will no doubt continue to keep pace with changing technology, market demands and other factors.

Overall, VLT gaming in Canada has matured since the early 1990s to become a stable, progressive program – providing meaningful returns to Canadians and balanced with social responsibility measures. It is well-positioned for the future – a future filled with more change and improvement still to come.



William P. Rutsey
President & CEO

Canadian Gaming Association

Executive Summary

HLT Advisory Inc. (“HLT”) was retained by the Canadian Gaming Association to research and document the historic development and current state of Video Lottery Terminal (“VLT”) gaming activity in Canada. Hereunder is a summary of the findings contained in the Report.

VLT gaming in Canada:

- Is well regulated, and operated honestly and transparently by Crown agencies;
- Offers entertaining, fair games in safe, age and access-controlled environments; and
- Raises significant non-tax revenues to fund key government programs and initiatives

The Canadian gaming industry is at the forefront of responsible gaming programs. Based on the most recent Canadian Gambling Digest, Canadian provinces currently spend approximately \$62.0 million on problem gambling treatment, research and awareness prevention initiatives. In addition, over \$13.0 million is spent in the area of responsible gambling initiatives.

Specific to VLT gaming, all provinces offering this form of gaming have developed and implemented responsible gaming programs that include both general messages and specific features installed on the VLT terminals themselves. Program and machine features include permanent on-screen clocks, wagering amounts displayed in actual dollars, pop-up reminders that display time spent on machine, problem gambling helpline phone numbers, restrictions on advertising, access and viewing, and staff training programs to recognize problem gambling signs. Further, these features are continually being researched and modified to increase their effectiveness.

While the number of illegal VLT-type machines is difficult to substantiate, it is the assessment and repeatedly expressed judgment of Canadian law enforcement agencies that this type of illegal gaming exists, and was more widespread prior to the introduction of regulated legal VLT gaming.

Those opposed to gaming often cite the experience in South Carolina as typical of VLT gaming in Canada; this comparison is unfounded. Video poker was operated in South Carolina in an uncontrolled and unregulated environment, by individuals and organizations not subject to any licensing, scrutiny or oversight. There was no effective regulation preventing children from playing the machines and individuals/businesses with criminal histories from owning/operating them. The experience in South Carolina stands in stark contrast with the current reasoned and well thought out pro-active approaches and programs operating in Canada.

Since 1991 VLT gaming in Canada has generated over \$25.0 billion in win. Provincial governments received approximately \$18.0 to \$19.0 billion of this total.

VLT gaming programs in Canada have been built upon certain principles (economic development, combating illegal activities and generating non-tax government revenues), sound rules and regulations and consistent distribution and economic models.

VLT gaming programs have not been static. Rather, they have been developed and modified to address changing circumstances, including market demand, improvements in technologies, research and public opinion:

- VLTs are restricted to age-controlled establishments.
- The number of machines and/or sites are periodically reviewed and adjusted.
- Responsible gaming features have been and will continue to be implemented.

There is an overall standard economic model for VLT programs in Canada

- All are operated by a provincial government controlled crown corporation and/or agency.
- All provinces retain the majority of revenue (70.0 to 85.0 percent of win).
- All provinces pay for capital and virtually all operating costs.
- All provinces direct revenues to general revenue funds and/or specific programs or areas, such as health and education.

All provincial VLT programs follow a general gaming distribution model based on population distribution throughout their respective jurisdictions. This model provides all residents with a similar degree of opportunity or accessibility to game if they so choose. With regard to combating illegal gaming, this distribution model also ensures that all residents have access to a legal form of gaming, and as such, an alternative to illegal gaming. The distribution model is also consistent with the cited economic development initiative of certain provinces, which focuses on direct financial assistance to local hospitality businesses. The VLT gaming distribution model is virtually the same as the lottery gaming model used by all provinces in Canada, except for the restriction limiting installation to age-controlled liquor licensed establishments.

The Canadian gaming industry is both broad and diverse and present in every region. What varies by region is the make-up of the industry (different mix of gaming activity). The industry has not been static. Rather, it has evolved with new products and new facilities being developed to meet market demand, changing consumer tastes and societal change. Over the last 10 to 15 years, casinos have been the driving force behind this industry growth and evolution, followed by VLT gaming and other electronic gaming devices ("EGDs"). Today (2005) the industry is over \$14.0 billion in size as measured by win. VLTs account for almost 22.0 percent of this total.

1. Introduction

HLT Advisory Inc. ("HLT") was retained by Canadian Gaming Association ("CGA") to research and document the historic development and current state of Video Lottery Terminal ("VLT") gaming activity in Canada. The report that follows summarizes our findings.

1.1 DEFINITION OF VLT GAMING

For the purpose of this report, VLT gaming is defined as the operation of a collection of electronic gaming devices located in age controlled hospitality establishments. For greater clarity, this does not include electronic gaming devices located in casinos, horse racetrack facilities ("racinos"), or bingo halls. Currently VLT gaming is operational in Alberta, Saskatchewan, Manitoba, Québec, New Brunswick, Prince Edward Island, Nova Scotia and Newfoundland and Labrador.

1.2 PURPOSE OF REPORT

The purpose of this report is to research and document the historical development and current state of VLT gaming activity in Canada. Although this report is not a study or analysis of responsible gaming, the report does include a compilation of responsible gaming programs and policies undertaken by the various provincial government agencies that operate and regulate VLT gaming. Information regarding American jurisdictions that offer VLT-style gaming is also included to compare and contrast with the Canadian experience and to better understand VLT gaming in Canada.

1.3 SCOPE OF WORK

The focus of the research undertaken to complete the document centered on explaining the broad historical development of VLT gaming in Canada. Specifically, this included:

- The rationale for VLT implementation;
- The economic models that have been adopted;
- The distribution models that guided implementation; and
- Regulations that guide operations.

The research is based primarily on published secondary information/data supplemented with selected discussions with industry officials. Appendix A provides a bibliography of information sources.

Please note that this report uses “win” to measure all gaming activity. Win is defined as “wagering less prizes” or that share of wagering that the gaming operator retains (before any taxes, site commissions and other operating expenses) for providing gaming activity that customers can participate in. In terms of VLT gaming, win can be defined as “money put in the machines minus money paid out”.

Note: The majority of Canadian gaming win data is collected on a fiscal year end basis, with year end being March 31st (i.e., in this report “2005” indicates the period beginning April 1, 2004 and ending March 31, 2005, unless stated otherwise). Pari-mutuel and some bingo and other charitable gaming (charity raffles, break-open tickets, etc.) data are collected on a calendar year end basis.

1.4 ORGANIZATION OF REPORT

Following the introduction, the report is organized in three sections.

- Section 2 provides an overview of the entire Canadian gaming industry. VLT gaming is a component of the entire gaming industry. While gaming activity is available in all provinces, each province has a unique mix of gaming activity. This mix is a function of many factors including government policy, population totals and distribution, historic evolution and consumer preference.
- Section 3 provides a statistical summary of the evolution of VLT gaming in Canada in the context of each province that offers this gaming activity, as well as relevant US jurisdictions.
- Section 4 provides a summary of VLT gaming programs in Canada in terms of the implementation rationale, regulations, distribution models and economic models. An overall report summary is also contained in this section.

Appendix A attached provides a bibliography of information sources.

2. The Canadian Gaming Industry

The Canadian gaming industry is made up of many different gaming activities, one of which is VLT gaming. In an attempt to shed light on the size and role of VLT gaming, this section of the report presents an overview of the entire Canadian gaming industry.

Note: The following information and data on the Canadian gaming industry as compiled by HLT does not generally include all temporary casino events (i.e., "Monte Carlo nights") or charity lottery events (i.e., hospital lotteries, etc.) and in some cases where data is not readily available, HLT has estimated this data based on partial information and experience in the Canadian gaming industry.

2.1 INDUSTRY DEFINITION

The Canadian gaming industry is both broad and diverse, having evolved over the last thirty-odd years into a multi-billion dollar industry. Much of this development and growth has taken place over the past 15 years with the introduction of new gaming activity.

While there is little debate on what constitutes gaming activity, there is some variation on classifying the various gaming activities that make-up the industry as a whole. Much of this classification variation has been directly related to local circumstances and government policies (i.e. many jurisdictions only permit the operation of certain types of gaming activity and as such they have classified gaming activity to fit into government policy). Some of these classifications are based on:

- Who operates (and/or who receives gaming profits from) the activity – i.e. charity gaming, commercial gaming, First Nation gaming;
- Types of electronic gaming devices – i.e. slot machines, video lottery terminals, video poker machines;
- Types of facility – i.e. Racino (gaming devices located within a racetrack facility), casino (table and electronic gaming devices), bingo hall, community gaming centre, etc; and
- Operating rules and regulations – i.e. "low stakes/high stakes", "coin in/paper out", etc.

In Canada, it is becoming increasingly difficult to describe the industry based on these types of classifications. For instance:

- Governments have and continue to redefine how charities and commercial operators receive a share of gaming proceeds;
- Technology advances are making it difficult to distinguish between different electronic gaming devices;

**Exhibit 2.1
Gaming Availability in Canada by Sector**

Province	Bingo	Casino	EGDs		Lotteries	Pari-Mutuel
			VLT	OTHER		
Newfoundland	●	---	●	---	●	●
Prince Edward Island	●	---	●	●	●	●
Nova Scotia	●	●	●	---	●	●
New Brunswick	●	---	●	---	●	●
Quebec	●	●	●	●	●	●
Ontario	●	●	---	●	●	●
Manitoba	●	●	●	●	●	●
Saskatchewan	●	●	●	●	●	●
Alberta	●	●	●	●	●	●
British Columbia	●	●	---	●	●	●

Source: HLT Advisory Inc.

- Facilities are changing as different gaming and non-gaming activity are being combined “under the same roof”; and
- Rules and regulations have and continue to be modified to keep pace with new developments.

In summary, gaming activity in Canada is not static but continues to evolve. With this said, HLT believes it is still useful to define the industry in terms of five broad sectors. These sectors are based on a combination of the primary gaming activity and location and/or facility that the activity takes place in. The resulting broad sectors are:

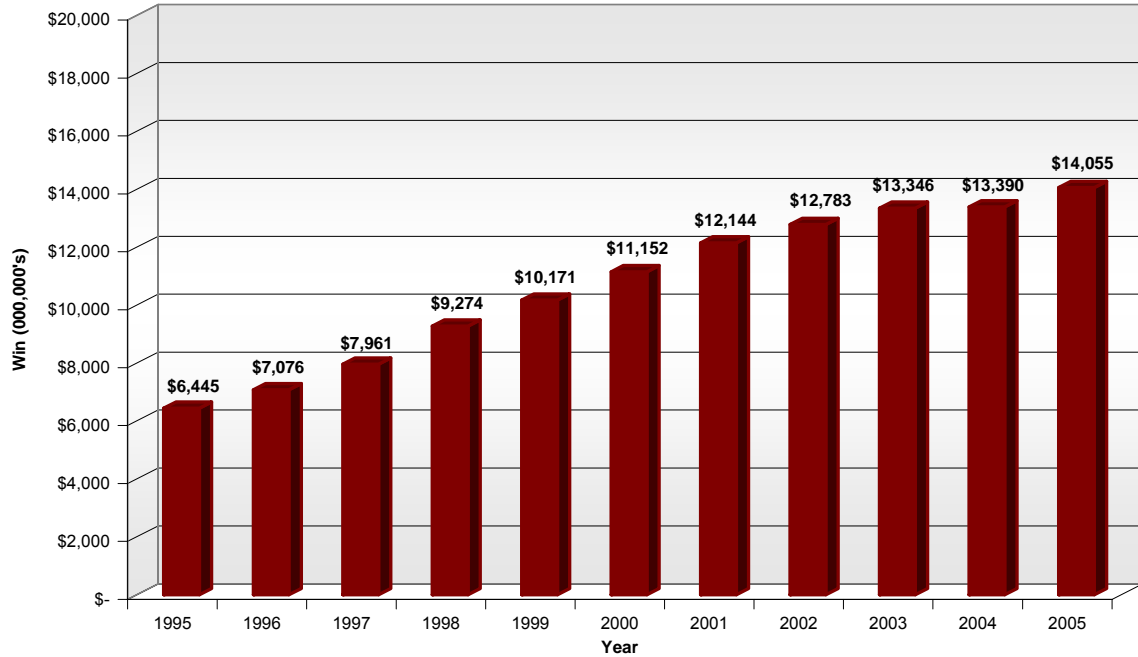
- Bingo;
- Casinos;
- Electronic Gaming Devices (“EGD”);
- Lotteries; and
- Pari-Mutuel (horseracing).

EGD refers to the operation of electronic gaming devices outside of traditional casinos. For the purposes of this report, the gaming activity within this sector can be further classified based on facility – those where gaming activity is the primary activity and those where gaming activity is ancillary to the non-gaming activity. VLT gaming activity falls into this latter classification while EGDs located at horse racetrack facilities (“racinos”) fall in the former classification (see report definition of VLT gaming in Section 1.1).

2.2 GAMING AVAILABILITY IN CANADA

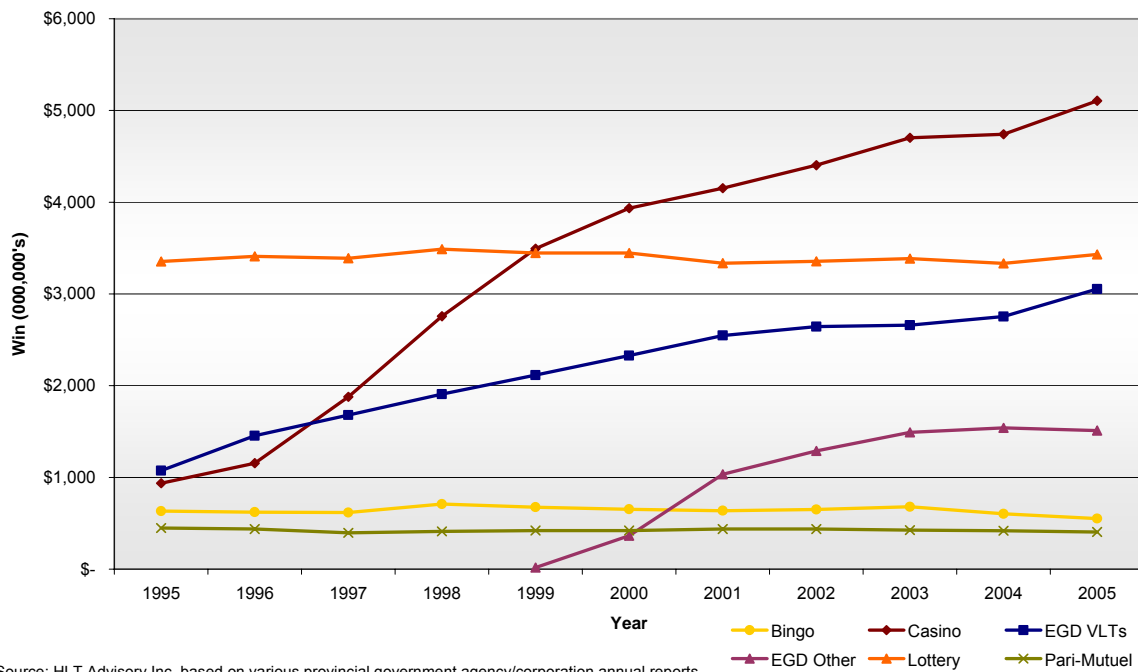
As depicted in Exhibit 2.1 facing, all of the provinces today offer a broad range of gaming activity for both residents and visitors to participate in. With regard to VLT gaming, eight of the ten provinces allow VLT gaming. While Ontario and British Columbia do not permit VLT gaming, they do permit EGDs at racetrack facilities (termed “Slots at Racetrack” in Ontario and “Racetrack Casino” in British Columbia). Of the provinces that permit VLT gaming, Québec, all of the Western Provinces and Prince Edward Island (Charlottetown Driving Park Entertainment Centre) also permit EGDs at racetracks. In the rest of Atlantic Canada, EGDs are not located at horse racetracks. British Columbia has recently permitted EGDs to be installed at certain bingo halls in the Province (these bingo halls are termed “Community Gaming Centres”).

Exhibit 2.2
Canadian Gaming Industry Win Trends



Source: HLT Advisory Inc. based on various provincial government agency/corporation annual reports.

Exhibit 2.3
Canadian Gaming Industry Win Trends by Sector

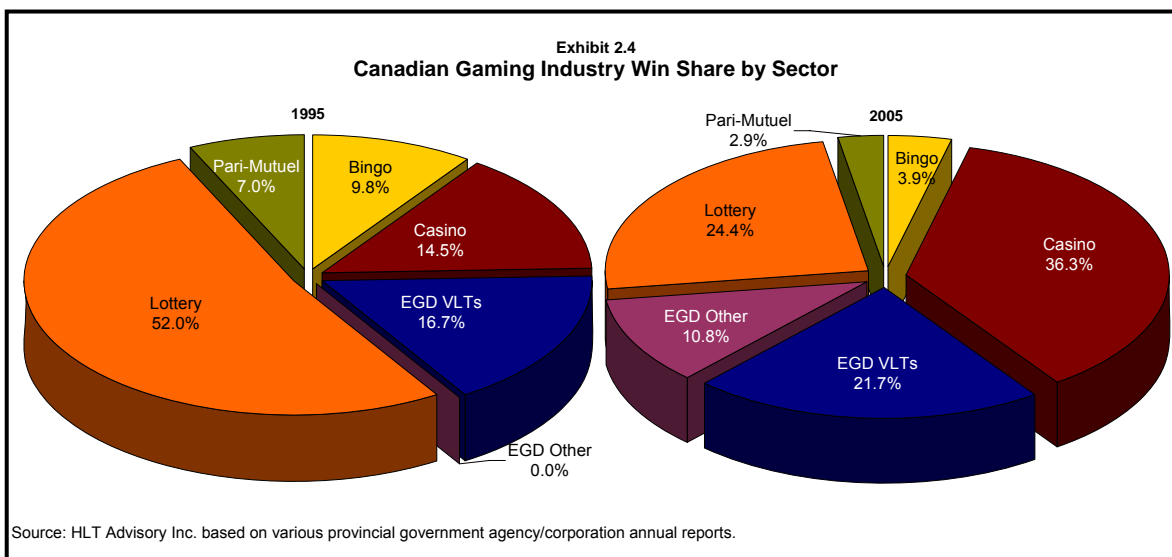


Source: HLT Advisory Inc. based on various provincial government agency/corporation annual reports.

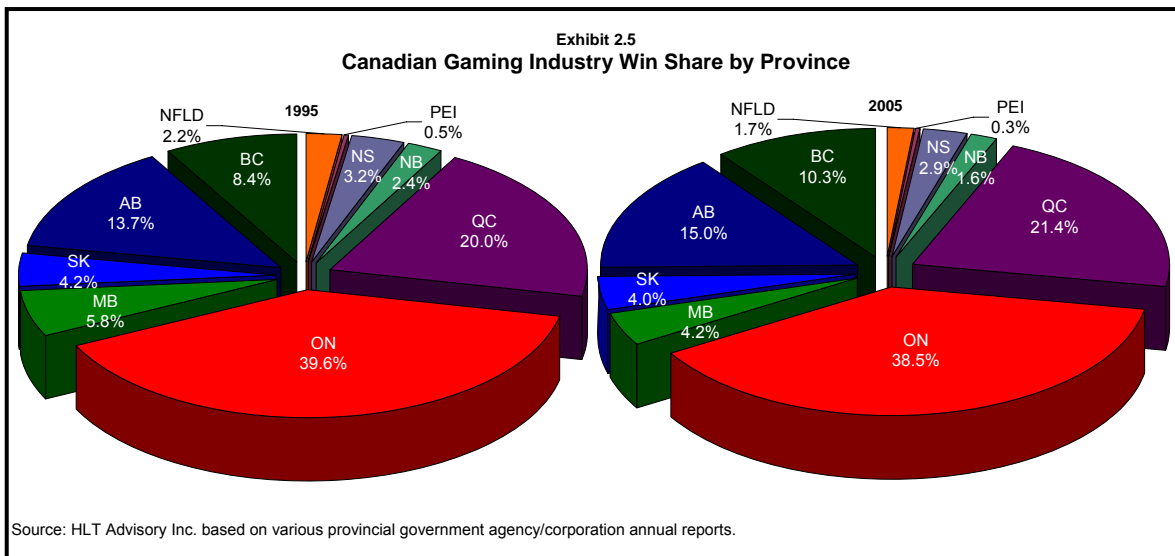
2.3 INDUSTRY AND SECTOR TRENDS

As shown in Exhibit 2.2 facing, the Canadian gaming industry has more than doubled in size since 1995 in terms of win. Today (2005), the industry is over \$14.0 billion in size. From a sector perspective (see Exhibit 2.3 facing), casinos followed by lotteries, VLT and Other EGDs are the largest sectors. From a trend perspective, the performance of lotteries has been relatively stagnant over the past ten years, while casinos have experienced the most rapid growth. VLT gaming experienced steady growth year over year from 1995 to 2001, followed by a period of stable performance (2001-2003). As detailed in Section 3.0, VLT gaming across Canada experienced a 14.7 percent rate of growth (almost \$400.0 million) from 2003 to 2005. Growth occurred in every province that has VLT gaming.

As shown in Exhibit 2.4 following, the Canadian gaming industry was dominated by lotteries in 1995 (over 50.0 percent of market share). By 2005, lotteries' share decreased by over half while casinos more than doubled its share of the entire market. VLT gaming increased its share of the market from 16.7 percent to 21.7 percent. Other EGDs (mainly Slots at Racetrack in Ontario) were implemented in the late 1990's and by 2005 accounted for 10.8 percent of the entire Canadian gaming industry.

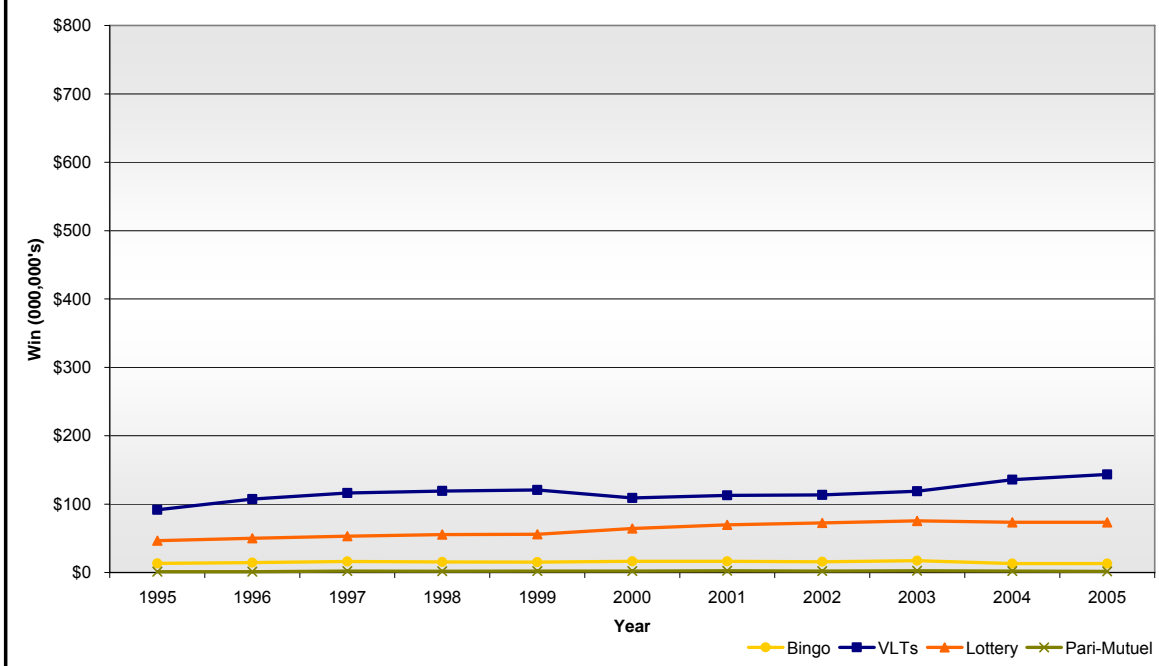


From a provincial perspective, the distribution of gaming industry win by province in 2005 virtually mirrors the distribution in 1995 (see Exhibit 2.5 following). This win distribution also generally mirrors Canada's population distribution. For instance, in 2005 Ontario and Québec accounted for 62.0 percent of Canada's total population and 59.9 percent of Canada's total gaming win. Atlantic Canada accounted for 7.4 percent of population and 6.5 percent of gaming win. Western Canada accounted for 30.2 percent of population and 33.6 percent of gaming win. What has varied between regions has been the types of gaming activities that are offered to customers.



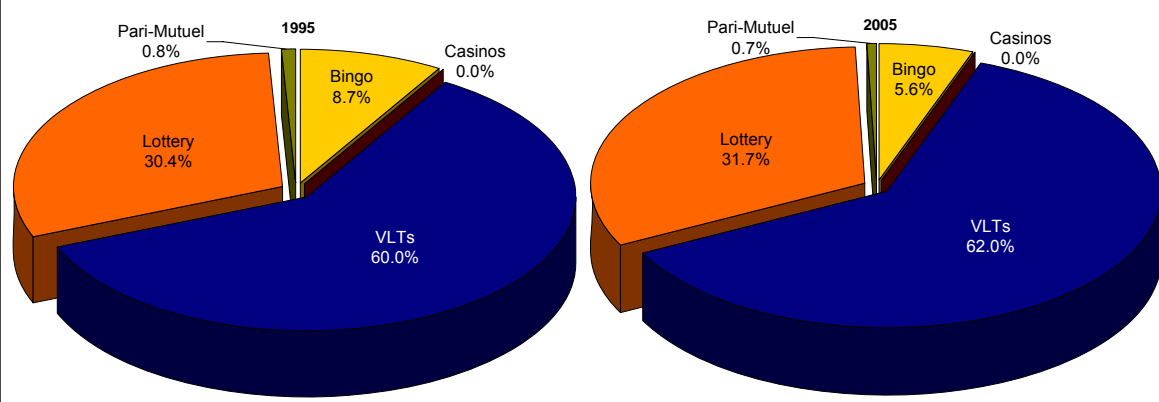
In conclusion, the Canadian gaming industry is both broad and diverse and present in every region. What varies by region is the make-up of the industry (different mix of gaming activity). The industry has not been static. Rather it has evolved with new products and new facilities being developed to meet market demand, changing consumer tastes and societal changes. Over the last 10 to 15 years, casinos have been the driving force behind this industry growth and evolution, followed by VLT gaming and other EGDs.

Exhibit 3.1
New Brunswick Gaming Industry Win Trends by Sector



Source: HLT Advisory Inc. based on various provincial government agency/corporation annual reports.

Exhibit 3.2
New Brunswick Gaming Industry Win Share by Sector



Source: HLT Advisory Inc. based on various provincial government agency/corporation annual reports.

3. VLT Gaming Activity by Jurisdiction

This section of the report describes the historical evolution of VLT gaming in Canada on a province-by-province basis together with the six US jurisdictions similarly authorizing and regulating VLT gaming, as well as South Carolina, where VLTs were operated in the 1990's and then banned in 2000. While all provinces in Canada began studying VLT gaming in the late 1980's and early 1990's, Atlantic Canada provinces were the first to introduce this form of gaming activity (New Brunswick was the first) followed by the three prairie provinces and then Québec.

Total gaming for each province is set out in terms of broad trends and market share by sector, followed by VLT gaming specific key developments since inception and key performance measures (win, number of machines, and number of locations).

Note: To facilitate province by province comparisons, the data scales in all the Exhibits in this section have generally been held constant, except for Québec. The size of Québec's gaming industry (and population compared to the other provinces that have VLT programs) necessitated the use of a larger scale.

3.1 NEW BRUNSWICK

The total gaming industry in New Brunswick has grown from approximately \$153.0 million in 1995 to over \$231.0 million in 2005. Over this time period, VLT gaming and lotteries accounted for the largest share of industry-wide growth. In 2005 VLTs accounted for 62.0 percent of New Brunswick's industry while lotteries accounted for 31.7 percent (see Exhibits 3.1 and 3.2 facing). Both of these shares are up slightly from 1995 totals. New Brunswick currently does not permit casino gaming.

New Brunswick was the first province to implement VLT gaming in Canada (December 1990). According to the Government of New Brunswick's 1997 *Video Lottery Program Review*, the Province began investigating the legalization of VLT gaming in 1988. At the time, as no other province in Canada had implemented this gaming activity, New Brunswick looked to US jurisdictions (Montana and South Dakota that at that time had legalized VLT gaming) to develop models and regulations. The impetus to legalize VLT gaming was a combination of revenue generation and to counteract the presence of illegal, unregulated VLT gaming in the Province (the government of the time estimated that between 5,000 and 7,000 illegal machines were in operation throughout the Province). These illegal machines had no age restrictions and were located in restaurants, service clubs, garages, bars, convenience stores and shopping malls. Neither payouts nor the size of bets were regulated. Credit and cheque cashing were thought to be common occurrences.

In 1990 a group of business people submitted a proposal to the government regarding the establishment and operation of a legal VLT program. The government entertained this proposal because they saw the need for help from the private sector to curb illegal gaming as well as deciding that there was no benefit to tax payers in owning and maintaining the machines themselves (\$6,000 to \$8,000 initial capital cost to purchase a machine). The proposal called for VLT win to be split between site holders (35.0 percent), VLT owners (35.0 percent) and the government (30.0 percent). Machines were distributed throughout the Province based on a maximum of five per qualified liquor licensed establishment and two per non-liquor licensed retail outlet. The government was not responsible for any operating costs, but did regulate, monitor and enforce compliance with the law through the Atlantic Lottery Corporation ("ALC") and the New Brunswick Lotteries Commission. New Brunswick is an equal shareholder (with all other Atlantic Canada provinces) of ALC.

In 1997 the Province undertook a review of the entire VLT program. A major focus of this review was the interpretation of results of public surveys conducted in 1992 and 1996. A series of recommendations regarding business economics and social considerations were put forward. These recommendations led to amendments to the VLT program being announced in 1998. The most significant amendment to the VLT program was the phasing out of VLTs in non-liquor licensed establishments (complete ban as of October 1, 1999). At the same time the government announced that ALC would take over the operation of the VLT network in 2002, replacing the VLT owners.

Since VLTs were implemented, the Province imposed changes to the revenue (win) distribution between the government, site holders and VLT owners (when they existed). In fact, nine such adjustments have increased the government's share of win from 30.0 percent in 1991 to 78.0 percent currently. Site holders saw their share (before applicable taxes) decrease from 35.0 percent in 1991 to 22.0 percent currently. VLT owners saw their share (before applicable taxes) decrease from 35.0 percent in 1991 to 24.0 percent in 2002, the last year they played a role in VLT gaming. It should be noted that prior to this time the VLT owners paid for all capital and operating costs out of their share of win. Post 2002 ALC has been responsible on behalf of the Province to pay all capital and operating costs.

In 1999 another significant development took place. The government undertook to hold a referendum on whether or not New Brunswick should continue its VLT program. The results of the subsequent referendum in 2002 maintained the status quo – VLTs being permitted to operate in liquor licensed establishments (maximum of 5 VLTs per site).

Exhibit 3.3 following illustrates the history of VLT gaming in New Brunswick in terms of win and number of VLTs in operation. As shown, the number of VLTs in operation grew from 1,984 in 1991 to 3,754 in 1997. Since 1997 the number of VLTs generally declined year over year to 2,639 in 2005. Win levels increased year over year until 1999 (\$120.7 million). After declining to \$108.8 million in 2000, win levels increased to \$143.3 million in 2005. The number of VLT locations increased from 1,211 in 1991 to 1,628 in 1997. By 2000 (the year VLTs were completely removed from non-liquor licensed establishments) the number of locations decreased to 755. Since 2000 the number of locations has decreased to 644 (by 2005).

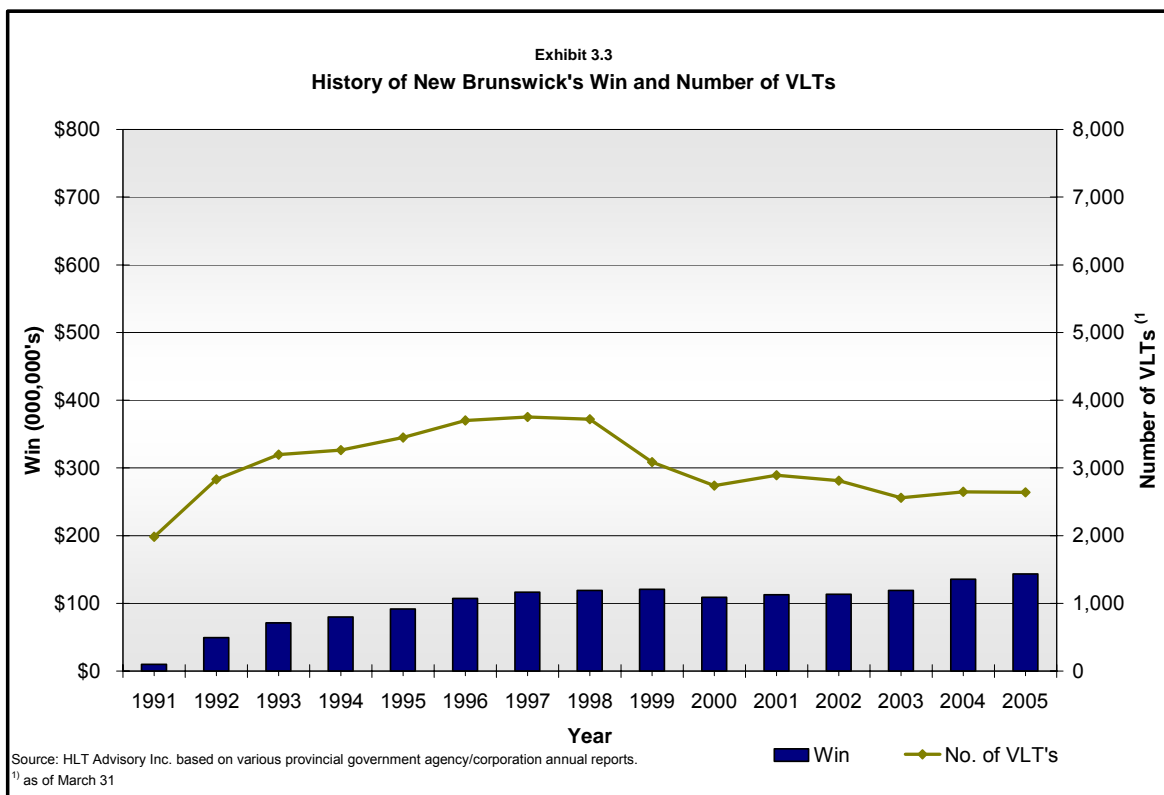
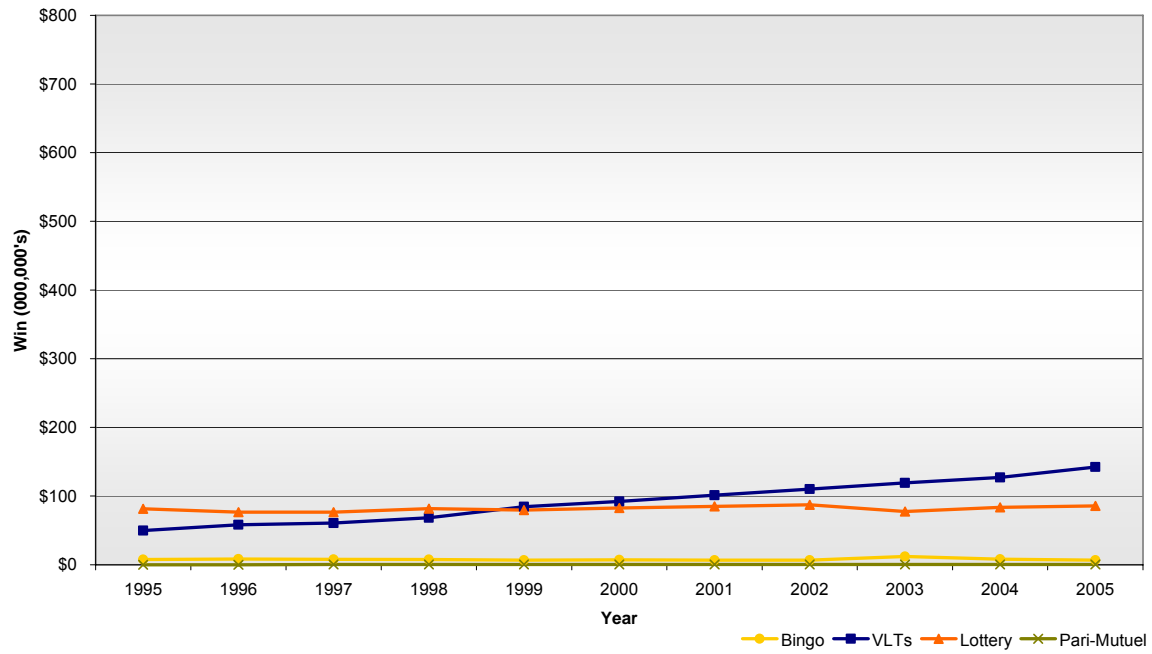
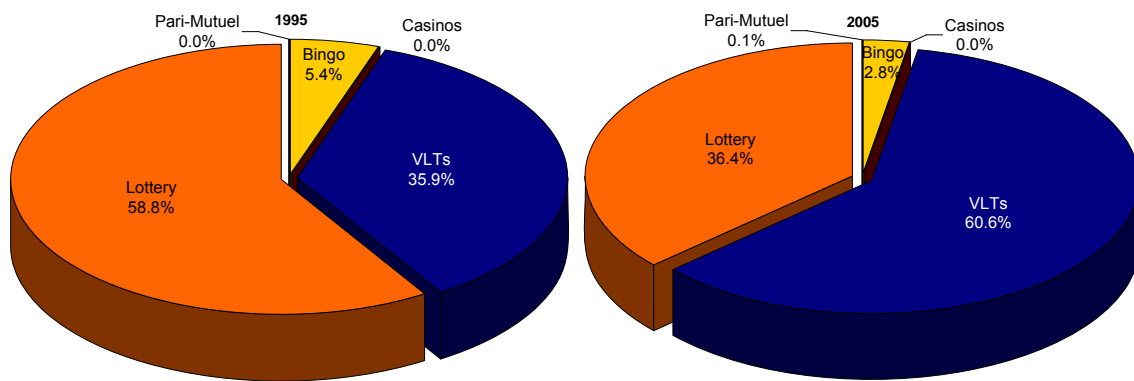


Exhibit 3.4
Newfoundland and Labrador Gaming Industry Win Trends by Sector



Source: HLT Advisory Inc. based on various provincial government agency/corporation annual reports.

Exhibit 3.5
Newfoundland and Labrador Gaming Industry Win Share by Sector



Source: HLT Advisory Inc. based on various provincial government agency/corporation annual reports.

3.2 NEWFOUNDLAND AND LABRADOR

The total gaming industry in Newfoundland and Labrador has grown from approximately \$139.0 million in 1995 to almost \$235.0 million in 2005. Over this time period, VLT gaming and lotteries accounted for the largest share of industry growth. In 2005 VLTs accounted for over 60.0 percent of the Province's total gaming industry while lotteries accounted for over 36.4 percent (see Exhibits 3.4 and 3.5 facing). Newfoundland and Labrador, like New Brunswick and Prince Edward Island, currently does not permit casino gaming.

Newfoundland and Labrador was the second province to implement VLT gaming in Canada (January 1991). Unlike New Brunswick, VLTs were only permitted to be installed in liquor licensed establishments (maximum of 5 VLTs per site). The VLT network is operated on behalf of the Province by ALC (of which Newfoundland and Labrador is an equal shareholder). The government retained 65.0 percent of win while site holders retained 35.0 percent (before applicable taxes). All capital and operating costs of the network are paid for out of the Province's share of win.

Since 1991, three changes to the initial revenue sharing arrangement have been imposed by the government. First in 1994, the government's share of win increased from 65 to 80.0 percent while the site holder's share decreased to 20.0 percent (before applicable taxes). Then in 1995, a two tier formula was imposed. Under this formula, the government would retain 73.3 percent of the first \$370,000 in annual win from all VLTs in a single site and 80.2 percent of win over \$370,000. In 1995 site holders began to contribute one percent of win from their share (before tax) to Gamblers Anonymous. The formula was revised in 1997 and again in 1998. This later formula (75.3 percent of the first \$400,000 and 80.2 percent over \$400,000) applies today.

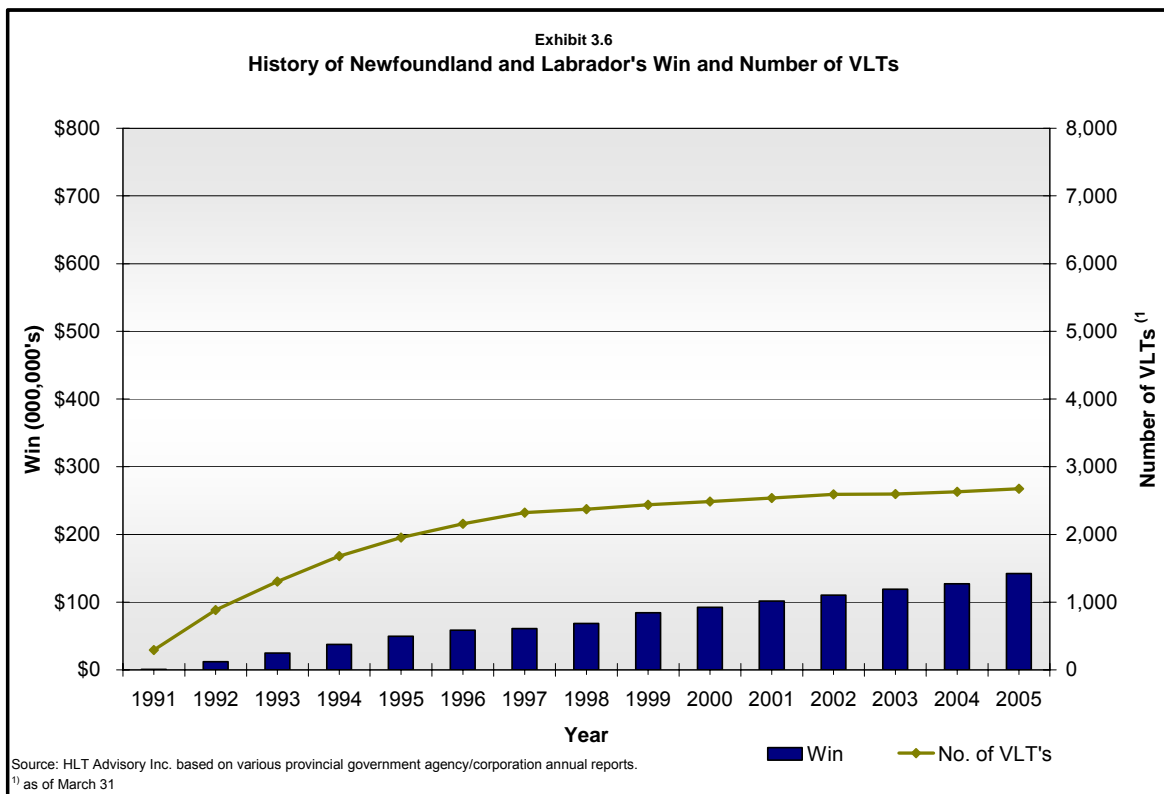
In 2005 the government announced a number of changes to its VLT program. These changes dealt with the number of machines permitted and new funding to enhance services for gambling disorders. In terms of the number of machines, the government froze the number at 2,687 and announced a five year reduction plan that would see the number of VLTs reduced by approximately 15.0 percent. This would decrease the number of VLTs to below 1997 levels (or approximately 2,280 machines). As part of this reduction, the government also announced they would stringently enforce the intent of the 1996 regulation that restricted sites to no more than 5 VLTs including the definition of a site. Since that time, a site had been defined as a liquor license. The government intends to change the definition to define a site as a physical location regardless of the number of liquor licenses that are at the physical location. Hence a site holder who has multiple liquor licenses at one physical location will be restricted to 5 VLTs in total.

In terms of new funding, the government announced that \$740,000 in new funding would be allocated to enhance services for gambling disorders. The targeted areas for this new funding would include:

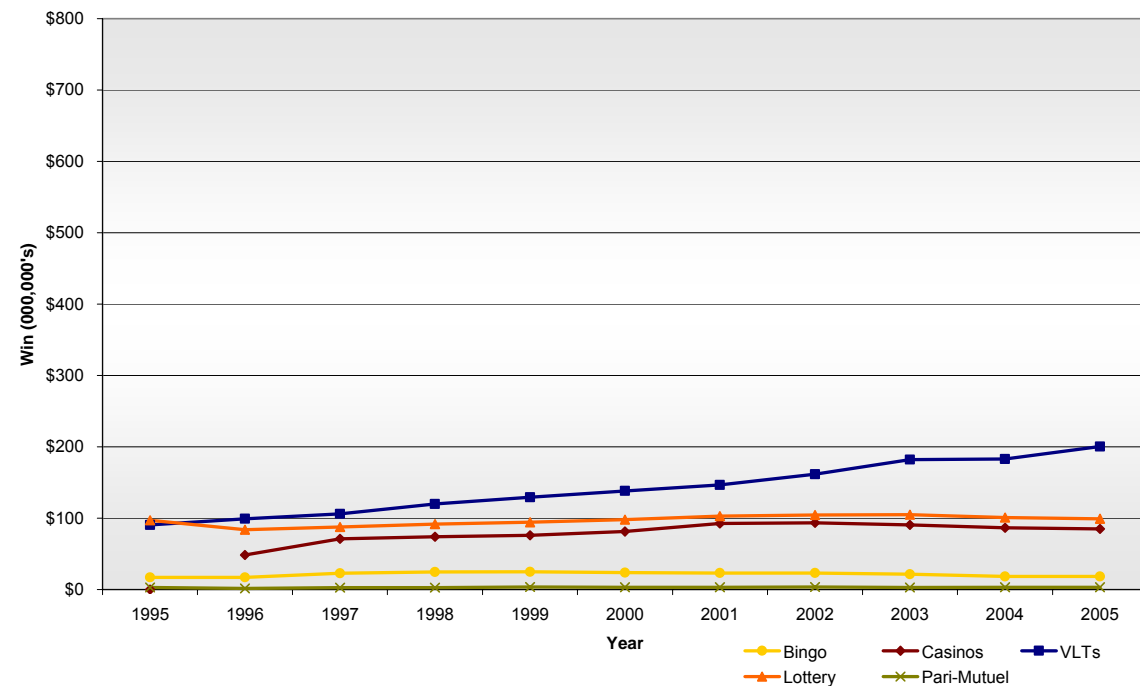
- Training for primary care physicians to screen and identify problem gambling;

- Enhanced public awareness with a campaign to inform individuals of the risks of gambling;
- Creating a provincial toll-free gambling counselling line based at Humberwood treatment centre in Corner Brook;
- Hiring five new addiction counsellors;
- Increasing the capacity of self-help and community groups to work with the formal system to address the issue of gambling in the community;
- Competency based training in gambling addictions for all addictions staff; and
- Completing a prevalence study to examine the incidence of gambling and problem gambling in the Province.

As shown in Exhibit 3.6 following, both win and the number of VLTs increased year over year between 1991 and 2005. In 2005 VLT gaming generated \$142.3 million in win from 2,675 machines in operation. The number of VLT locations also increased year over year from 265 in 1992 (the first full year of operation) to 593 in 2005. As mentioned previously, in 2005 the government froze the number of machines permitted to operate in the Province at 2005 levels and announced a five year reduction plan that would entail a 15.0 percent reduction in the number of VLTs in operation.

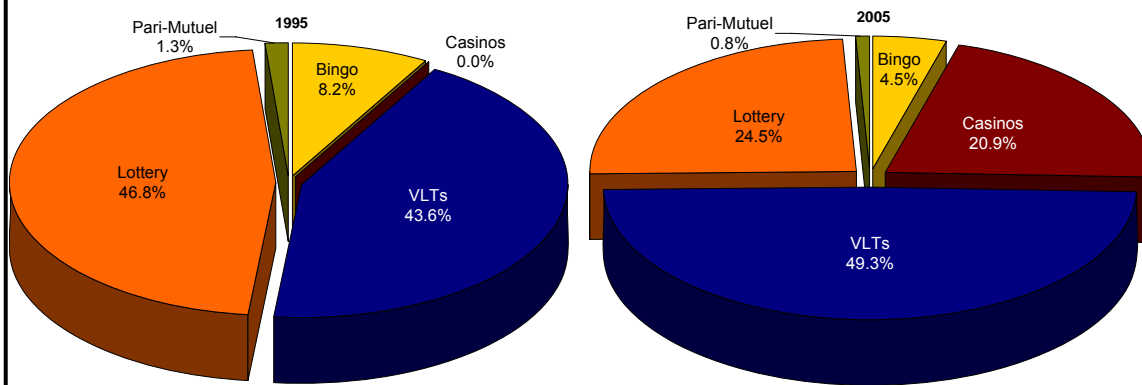


**Exhibit 3.7
Nova Scotia Gaming Industry Win Trends by Sector**



Source: HLT Advisory Inc. based on various provincial government agency/corporation annual reports.

**Exhibit 3.8
Nova Scotia Gaming Industry Win Share by Sector**



Source: HLT Advisory Inc. based on various provincial government agency/corporation annual reports.

3.3 NOVA SCOTIA

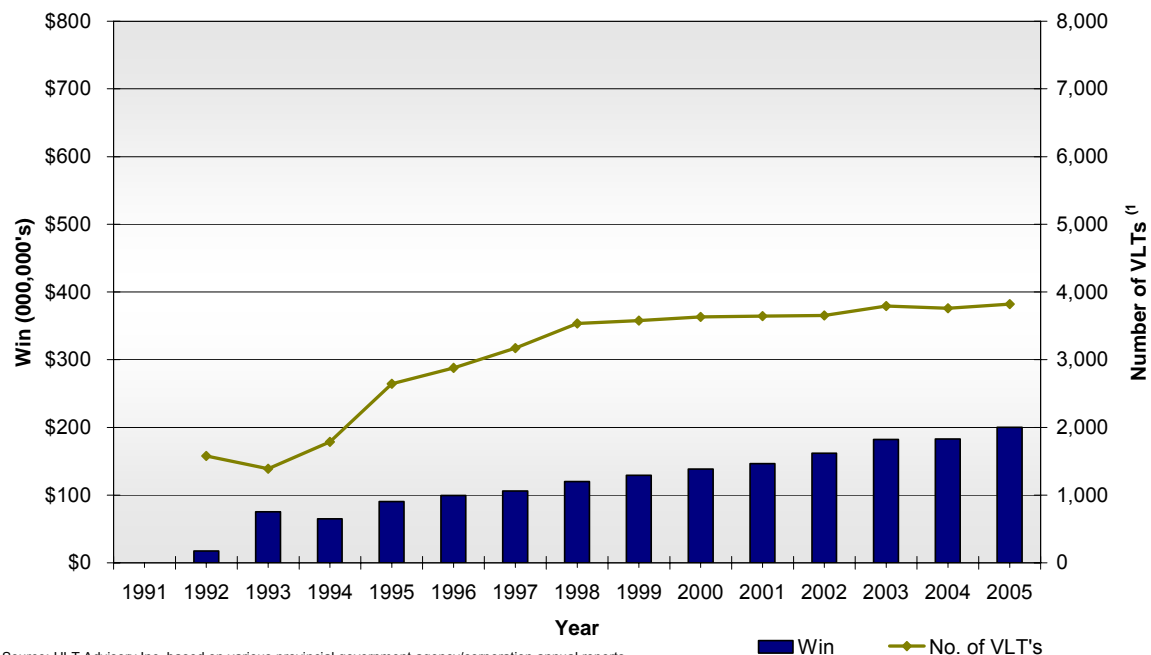
The gaming industry in Nova Scotia has grown from approximately \$208.0 million in 1995 to almost \$406.0 million in 2005. Over this time period, VLT gaming and casinos accounted for the largest share of Nova Scotia's industry growth. In 1995 lotteries accounted for the largest share of Nova Scotia's gaming industry at 47.0 percent. Casinos were introduced in 1996. By 2005, casinos accounted for almost 21.0 percent of Nova Scotia's gaming industries. VLTs increased its share of the Province's gaming industry from almost 44.0 percent in 1995 to approximately 49.0 percent in 2005 (see Exhibits 3.7 and 3.8 facing).

Nova Scotia launched its VLT program in May 1991. Nova Scotia decided to introduce a legal VLT program in part due to growing illegal gambling in the Province. Initially, VLTs were allowed in both liquor and non-liquor licensed establishments. Shortly after implementation (1993), in response to public criticism, the government restricted VLTs to liquor licensed sites.

Similar to Newfoundland and Labrador, Nova Scotia set up its VLT program with ALC as its operator (Nova Scotia is an equal shareholder of ALC). The government initially retained 65.0 percent of win while site holders retained 35.0 percent (before applicable taxes). All capital and operating costs of the network were paid for out of the Province's share of win. Since implementation of the program, the Province changed the "win split" four times. Currently (last change occurred July 1, 2004), all site holders except non-profit/social groups receive 24.75 percent (before applicable taxes) of win on the first \$400,000 from all VLTs in one site and 19.8 percent (before taxes) of win over \$400,000. Non-profit/social groups receive 24.75 percent (before taxes) of all win. The Province has a different revenue formula for First Nation VLTs whereby the First Nation receives all revenue less a flat fee of up to \$136 per VLT per week. This fee is essentially to offset network operation costs of the Province.

In 1998 the Province passed the *Video Lottery Terminal Moratorium Act*. This Act, still in effect, imposed a limit of 3,234 VLTs that can operate in the Province (excluding VLTs on First Nation lands). In June 2005, the Province reduced the operating hours of VLTs (excluding First Nation VLTs, all machines cannot operate past midnight). This reduction in operating hours in June was followed up with the removal of 800 machines from for-profit site holders in November (2005). Every VLT site holder with more than three machines lost a percentage of the machines at their site. A further 200 machines will be removed through attrition. These reductions combined represent an approximate 30.0 percent total reduction in the number of VLTs permitted to operate in the Province (3,234 to 2,234 VLTs excluding First Nations). The impetus for these reductions was the *Nova Scotia's Gaming Strategy (April 2005)*. This strategy focused on the entire Nova Scotia gaming industry.

Exhibit 3.9
 History of Nova Scotia's Win and Number of VLTs



Source: HLT Advisory Inc. based on various provincial government agency/corporation annual reports.

¹⁾ as of March 31

Since 1995 VLT site holders and the Province have contributed towards a VLT Problem Gambling Fund. The Fund was renamed the Nova Scotia Gaming Foundation in 1998. Since 1996 the Foundation has received annual funding of approximately \$750,000. In 1999 the Province launched the *VLT Retailer Responsible Gaming Program*. The Program focuses on informing VLT retailers (site holders) and their staff about problem gambling issues and responsible gaming strategies. In addition to this education program, the Province currently has a number of responsible gaming features on all VLTs in the Province. These features include:

- Pop-up reminders advising players how long they have been playing;
- Permanent on-screen clock reminding players of the actual time of day;
- Cash display vs. credits showing the player's wager in actual dollars, not credits; and
- Mandatory cash-out requirement cashes out the players winnings automatically at 150 minutes of play.

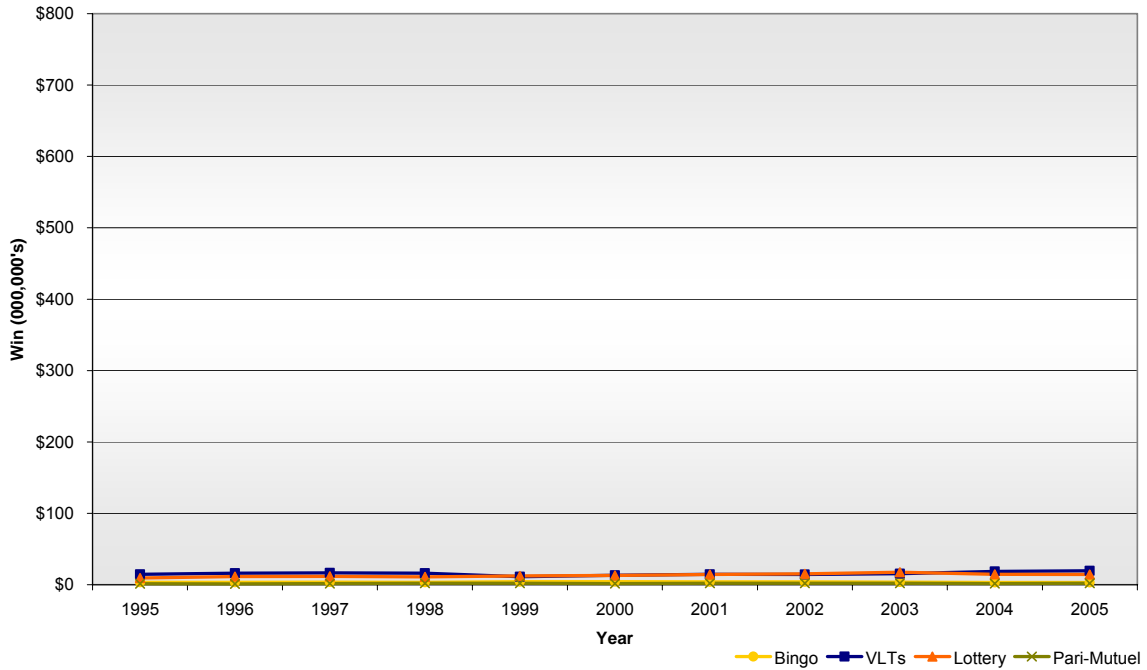
Also since 2001, the Province has invested in primary research to study the effectiveness of its responsible gaming program and specifically responsible gaming features for VLT machines. This research has included:

- Video Lottery Responsible Gaming Feature Research (October 2002)
- Responsible Gaming Feature Enhancements Study (October 2004)
- Nova Scotia VLT Self-Exclusion Report (2004)
- Nova Scotia Player Card Research Project, Stage 1 Research Report (September 2005)
- Nova Scotia VLT Time Change (November 2005)

Responsible gaming is also a major theme in the Province's overall gaming strategy (*A Better Balance: Nova Scotia's First Gaming Strategy*, 2005).

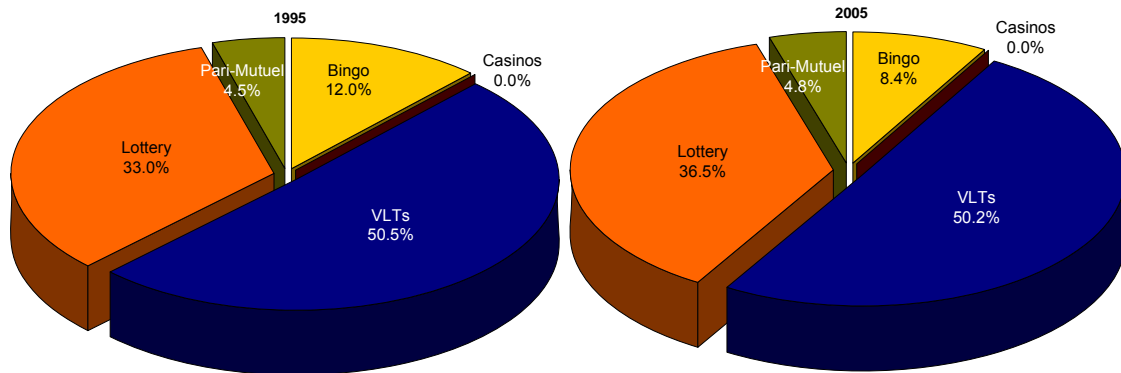
Exhibit 3.9 facing illustrates the history of VLT gaming in Nova Scotia in terms of win and number of VLTs in operation. (Note: the total number of VLTs includes VLTs in First Nation communities.) As shown, after removing VLTs from non-liquor licensed sites in 1993, the number of VLTs in operation has generally grown year over year. Increases after 1998 are solely attributed to First Nations. Since 1995 the Province entered into gaming agreements with various First Nations allowing them to install VLTs in their communities. Win from VLTs has increased year over year since 1994 reaching \$200.2 million in 2005. The recent reduction in the number of machines will be reflected in 2006 year end numbers. The number of VLT locations in the Province has increased year over year since inception, and currently (2005) stands at 593.

Exhibit 3.10
PEI Gaming Industry Win Trends by Sector



Source: HLT Advisory Inc. based on various provincial government agency/corporation annual reports.

Exhibit 3.11
PEI Gaming Industry Win Share by Sector



Source: HLT Advisory Inc. based on various provincial government agency/corporation annual reports.

3.4 PRINCE EDWARD ISLAND

The total gaming industry in Prince Edward Island has grown from approximately \$29.0 million in 1995 to just over \$39.0 million in 2005. Over this time period, VLT gaming and lotteries accounted for the largest share of Prince Edward Island's industry growth. In 2005, VLTs accounted for over 50.0 percent of Prince Edward Island's total gaming industry while lotteries accounted for almost 37.0 percent (see Exhibits 3.10 and 3.11 facing). Like New Brunswick and Newfoundland and Labrador, Prince Edward Island currently does not permit casino gaming. While Prince Edward Island does not currently permit casino gaming, it did recently approve the development of a "racino".

- In August 2005, 225 EGDs were installed at the Charlottetown Driving Park. The new gaming facility (EGD and horse racetrack components combined) has been renamed the Charlottetown Driving Park Entertainment Centre. The EGD component is operated by ALC on behalf of the Province. The horse racetrack component operator receives a share of the EGD win.

Prince Edward Island commenced the operation of its VLT program in August 1991. The program followed that of New Brunswick in terms of private sector ownership and operation of the machines. In 1991 the government received 50.0 percent of the revenue while site holders and VLT owners split the remaining revenue equally. The VLT owners covered all capital and operating costs. VLT owners participated in the VLT program up to 2003 after which ALC assumed responsibility for the supply, maintenance and technical support of the machines. Based on information contained in the Annual Report (March 31, 2003) of the Prince Edward Island Lotteries Commission, the change from private sector VLT owners to the ALC was done to bring the Province's VLT program in line with all other Atlantic Canada provinces (at this time, ALC was operating all of Atlantic Canada's VLT programs).

From 1992 to 2003 the government changed the revenue share formula four times increasing its share of win from 35.0 percent to 80.0 percent. Site holders saw their share decrease from 35.0 percent (before applicable taxes) to 20.0 percent. VLT owners started at 30.0 percent (before applicable taxes) and were phased out in 2003 after two separate reductions to their share.

In 1993 the government restricted the hours that VLTs were available to be played to between the hours of 11:00AM and midnight. Also, VLTs could not be played on Christmas Day, Good Friday or on any Sunday throughout the year. The Province further restricted VLT availability in 1996. In that year the Province introduced a cap on the number of VLTs allowed in the Province (615). Further, liquor licensed establishments could not have more than five VLTs per site and non-liquor licensed establishments could not have more than two. By 1998 the government removed all VLTs that were located in non-liquor licensed establishments.

Exhibit 3.12 following illustrates the history of VLT gaming in Prince Edward Island in terms of win and number of VLTs in operation. As shown, the number of VLTs and win generally increased year over year from inception in 1992 to 1998. In 1999, the first full year that machines were removed from non-liquor licensed establishments, the win dropped from \$16.2 million to \$11.4 million.

- *Note: VLTs were removed from non-liquor licensed establishments in March 1998, one month before the 1998 year-end. Hence the number of machines in operation at the end of 1998 (March 31, 1998) shows the reduced number of 379. For the majority of 1998 however, over 600 machines were in operation. The real impact on win from the reduction in VLTs was not experienced until 1999.*

Since 1999, while the number of machines in operation has generally ranged from 350 to 430, the win level has steadily increased from \$11.4 million to almost \$20.0 million. Between 1992 and 1997, there were generally 225 to 250 VLT locations per year in the Province. Once VLTs were banned in non-liquor licensed establishments the number of locations dropped to between 75 and 100 per year.

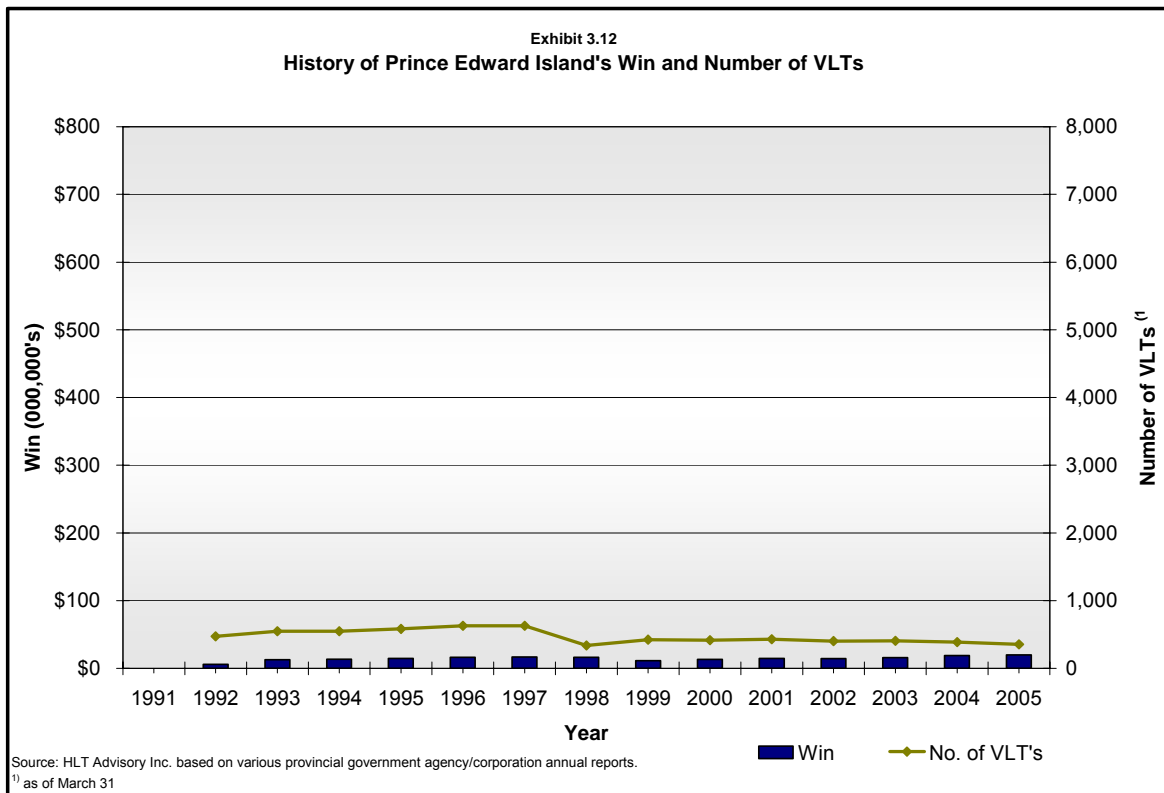


Exhibit 3.13
Manitoba Gaming Industry Win Trends by Sector

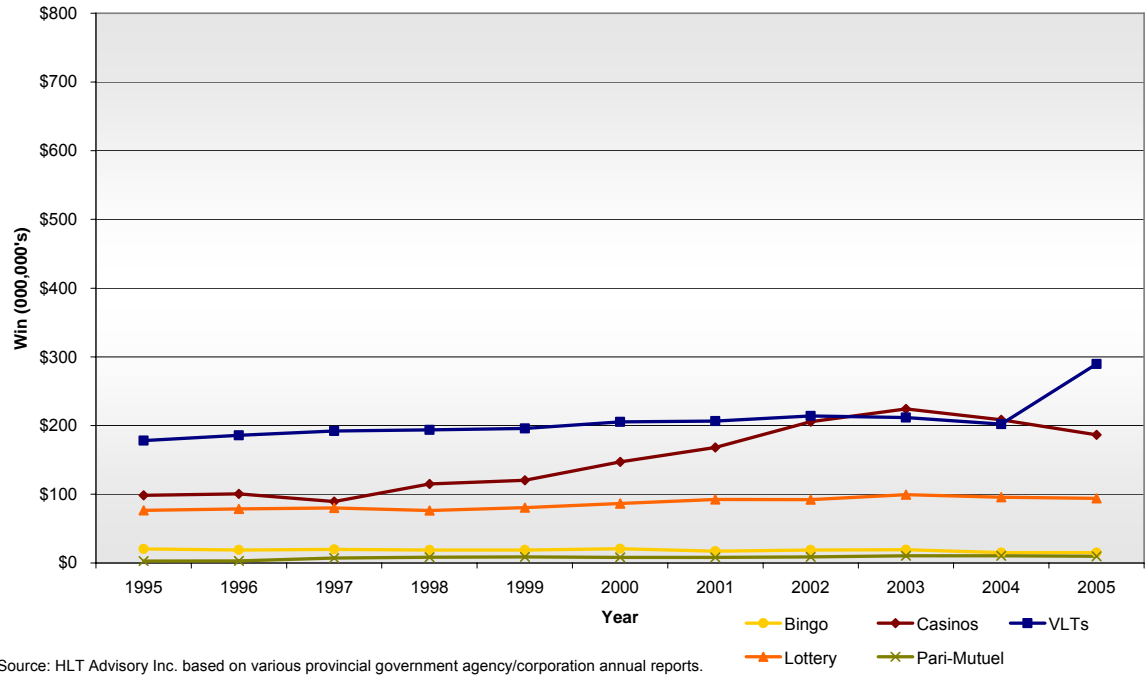
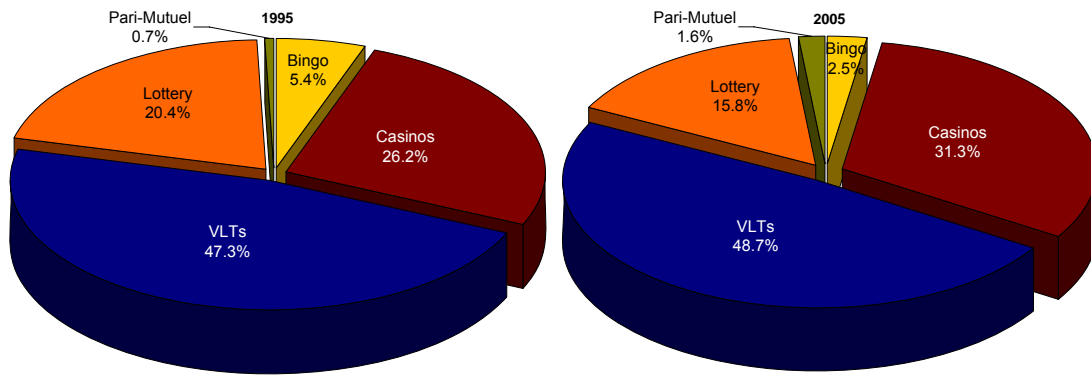


Exhibit 3.14
Manitoba Gaming Industry Win Share by Sector



3.5 MANITOBA

The total gaming industry in Manitoba has grown from approximately \$376.0 million in 1995 to over \$594.0 million in 2005. Approximately \$200.0 million of this growth is attributable to growth in casino gaming (closing of one casino and the opening of two other casinos including subsequent redevelopment of these two casino sites) and VLT gaming. Both of these sectors grew by approximately \$100.0 million each over the time period. VLT win grew by almost \$90.0 million between 2004 and 2005. This growth can be attributed to the replacement of VLT machines and the implementation of a smoking ban at the Winnipeg casinos during this time period. Between 1995 and 2005, VLTs retained their share of gaming win in Manitoba at around 48.0 percent while casinos increased their share from 26.0 to 31.0 percent. Lotteries had their share decrease from approximately 20.0 to 16.0 percent (see Exhibits 3.13 and 3.14 facing).

VLTs were first introduced in Manitoba in November 1991. The initial impetus of the VLT program was to support new rural economic development initiatives and as such VLTs were installed only in rural liquor licensed establishments. The program scope was expanded to include the City of Winnipeg in September 1993. Following the expansion of VLTs to Winnipeg, the government placed a moratorium on further expansion of VLT sites as well as casino sites.

In 1994 VLT-style gaming machines were installed at Assiniboia Downs horse racetrack in Winnipeg (considered part of VLT gaming sector for the purpose of this report). Manitoba Lotteries Corporation ("MLC") also launched a "mobile" VLT program for eligible fairs and special events as well as a seasonal program for Winnipeg riverboats.

In 1995 the government initiated a review of lottery and gaming policy in the Province ("The Lottery Policy Review Working Group"). During this review, the 1993 moratorium was upheld. By June of 1996 the government released an implementation plan based on the findings of the review. A significant recommendation led to the creation of the Manitoba Gaming Control Commission ("MGCC"), a commission responsible for regulating all forms of gaming in the Province. Directly dealing with VLTs, recommendations included:

- A 10.0 percent reduction in the number of VLTs;
- A reduction in the number of VLTs permitted at one site from 40 to a maximum of 30;
- A review of the VLT program every two years; and
- The imposition of regulations to limit the view of VLTs by minors.

In 1998 and 1999 MGCC created the *Gaming Control Local Option (VLT) Act*. This Act provided the framework to undertake community plebiscites with regard to VLTs. To date one community (Town of Winkler) has held a plebiscite whereby the results lead to the removal of all VLTs in that community.

Since 1999 the Province placed a greater emphasis on responsible gaming. With regard to the VLT program, VLTs in the Province were replaced in 2004. The new machines included a number of built-in responsible gaming features to enhance player controls and provide information, such as messages about a Problem Gambling Helpline and how gambling works. Other features included time limits on gaming sessions with mandatory cash-out, credits shown in dollar amounts, an on-screen clock and a maximum amount of money that can be inserted into a machine is \$60 per session.

Exhibit 3.15 following illustrates the history of VLT gaming in Manitoba in terms of win and number of VLTs in operation. As shown, the number of VLTs in operation increased rapidly up to 1995 (implementation phase) then declined through 1998. Since 1998, the number of VLTs has increased slightly from 4,889 to 5,369. The number of sites has remained relatively constant between 550 and 600 since 1995. Win initially increased rapidly up to 1995 and then grew only slightly from approximately \$178.0 million to \$202.0 million in 2004. The introduction of new machines in 2004 helped push win to almost \$290.0 million in 2005.

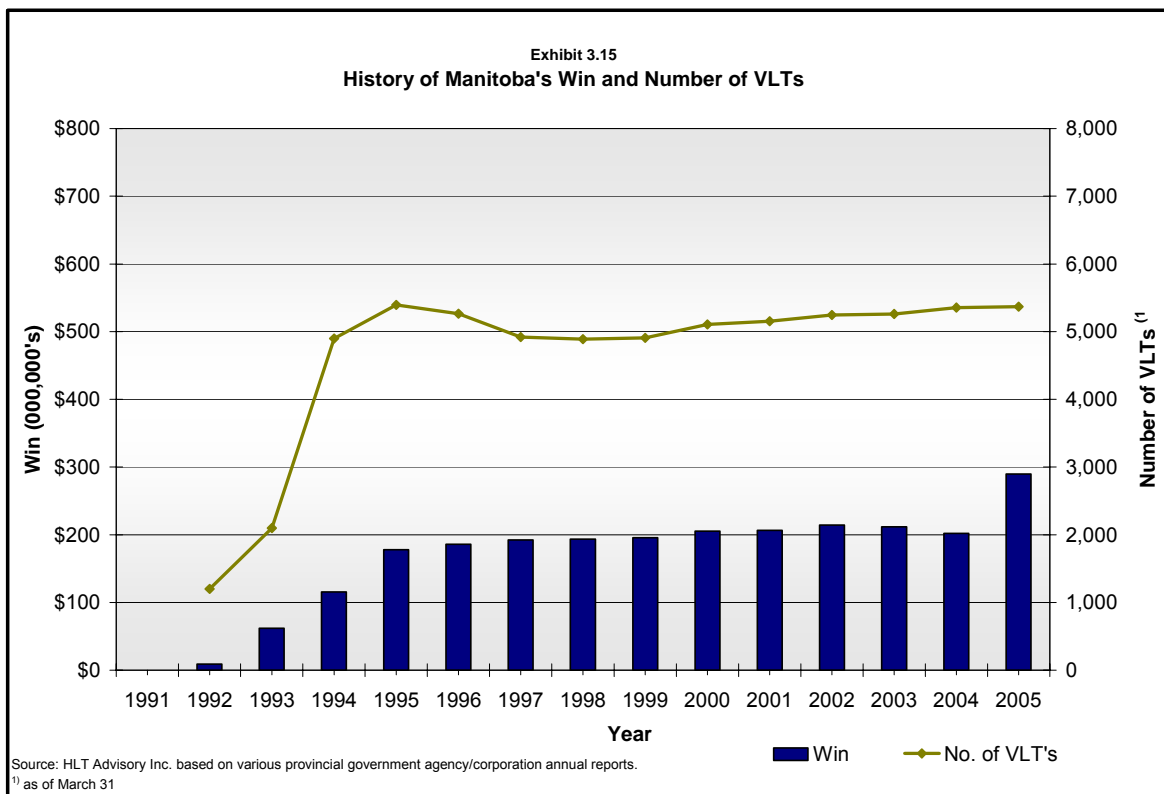


Exhibit 3.16
Alberta Gaming Industry Win Trends by Sector

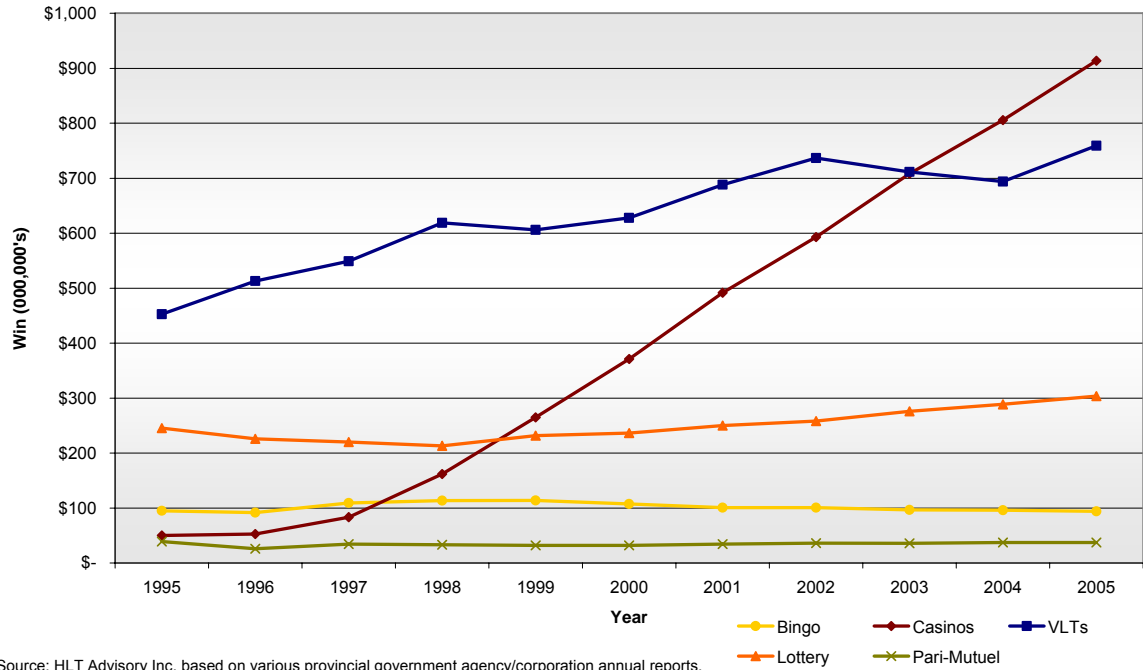
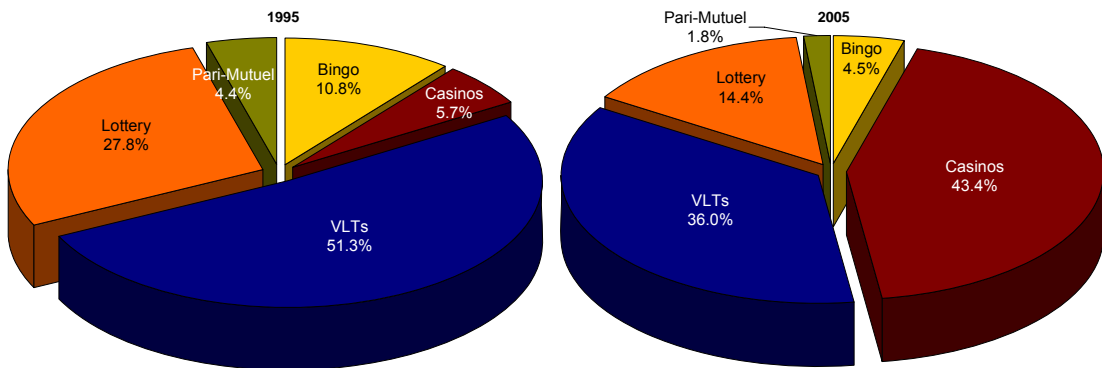


Exhibit 3.17
Alberta Gaming Industry Win Share by Sector



3.6 ALBERTA

Alberta's gaming industry more than doubled in size from approximately \$882.0 million in 1995 to over \$2.1 billion in 2005. Of this over \$1.0 billion increase, casinos accounted for approximately 70.0 percent, while VLTs accounted for approximately 25.0 percent. By 2005 casinos accounted for almost 42.0 percent of all gaming win in the Province followed by VLTs at about 36.0 percent. In 1995 VLTs accounted for over half of Alberta's entire gaming industry win (see Exhibits 3.16 and 3.17 facing).

Alberta began investigating starting a VLT network in 1991. It ran a ten day trial of VLTs at both the Calgary Stampede and Edmonton Klondike Days events. This was followed by a test in 30 age-controlled liquor licensed establishments throughout the Province. These tests proved positive and the Province launched its VLT program in March 1992. The rationale for this new gaming format in liquor licensed premises and special event days, was to generate revenue for the Alberta Lottery Fund and to prevent illegal gambling machines from gaining a foothold in the Province. The initial plan was to install some 8,600 VLTs over three years throughout the Province. The machines would only be permitted in liquor licensed establishments.

By 1994 the government formed the Lotteries Review Committee to consult with Albertans about the future direction of all gaming in the Province. In 1995 the Committee released its report; 13 recommendations regarding VLTs were made and included such things as:

- Continuing the province-wide cap of 6,000 VLTs;
- Allocating a portion of the VLT revenue back to communities through local lottery boards;
- Slowing down the speed of VLTS (speed of play);
- Allowing communities to decide by municipal plebiscite to prohibit VLTs in their community;
- Abolishing the incentive/bonus system for retailers (retail commission to be 15% of net sales); and
- Prohibiting VLT staff from playing when on duty.

The government subsequently adopted all the recommendations except the one related to speed of play. At the same time that the Lotteries Review Committee was conducting its review, the government commissioned the first research report regarding the prevalence of gambling and problem gambling among adult Albertans. The government also made the decision to fund the Alberta Alcohol and Drug Abuse Commission ("AADAC") to provide problem gambling treatment, research and prevention and education programs in Alberta. AADAC receives most of its funding from the Alberta Lottery Fund. In 2005-2006 almost \$63.0 million will be provided for prevention, treatment and education programs.

In 1996 the government amalgamated all agencies dealing with gaming and alcohol in the Province and created the Alberta Gaming and Liquor Commission ("AGLC") under the Gaming and Liquor Act.

Between 1997 and 1998 a number of municipal local plebiscites (40) voted on whether to remove VLTs from establishments located in their communities. A number of municipalities voted to remove VLTs while the majority voted to allow VLTs to stay in operation. While the government attempted to uphold the outcome of municipal plebiscites, it needed to pass specific legislation to do so. Bill 36 was passed in 1999 allowing the government to terminate VLT retailer agreements in municipalities that voted to have VLTs removed. Various legal challenges were initiated by VLT retailers to stop the removal. It was not until 2004 that these challenges were struck down and the government removed machines from those municipalities that voted to do so.

By 2002 the government adopted a policy from a *Gaming Licensing Policy Review* (a review that took place in 2000/01) in which 13 recommendations were made regarding VLTs. A number of recommendations addressed reduced accessibility to VLTs:

- Reduce accessibility and move towards a greater concentration of VLTs in fewer locations; and
- Allow dedicated VLT gaming venues with 15- 25 VLTs and operate under enhanced facility standards (based on performance, a multiple license facility with more than 10 VLTs could consolidate 15 to 25 VLTs into one gaming entertainment room referred to as a Video Gaming Entertainment Room ("VGER")).

These policies along with an increase to the number of VLTs permitted per license from 7 to 10 was designed to help reduce the number of locations offering VLTs in the Province over a three year period by 10.0 to 15.0 percent. By 2005 a 14.0 percent reduction had been achieved.

Also in 2002 the government initiated replacement of both the VLT central system and individual machines (completed by 2004) due to terminal age and obsolescence. The decision related to integrity of the gaming activity, entertainment value for customers and the incorporation of responsible gaming features in the new terminals. These new features targeted at-risk gamblers, problem gamblers and included reality checks for players (i.e., on-screen clock, timed pop-up messages to remind players how long they have been at the machine, winnings posted in dollar amounts as opposed to credits, and problem gambling helpline messages). The effectiveness of these features is being evaluated over a three year period. Other responsible gaming initiatives that were implemented (since 2000) included mandatory site retailer education programs, posting of signs related to problem gaming and gaming in general, and the provision of server intervention products (i.e., matchbooks, coasters, business cards). A 24-hour problem gambling help line was also introduced.

In 2004 within AGLC, a Social Responsibility Division was created to develop new problem gambling initiatives and policies based on research and consultation with industry and other jurisdictions. In addition, the Alberta Gaming Research Institute (“AGRI”), an entity formed in 1999 between the University of Lethbridge, Calgary and Edmonton, has received \$1.5 million from the Alberta Lottery Fund each year for the past six years to research gambling related issues including gaming trends, costs and benefits of gaming and problem gambling treatment and prevention.

Exhibit 3.18 following, illustrates the history of VLT gaming in Alberta in terms of win and number of VLTs in operation. As shown, the number of VLTs in operation increased rapidly until 1995 (implementation phase) then has been generally held constant just below 6,000, the cap imposed and upheld by the Province since 1995. The number of sites increased to over 1,200 by 1995 and remained above this total until 2003, the first year that the government imposed a three year reduction in the number of sites. Win initially increased rapidly until 1998. While win in total increased from 1998 to 2005, decreases were experienced during three years over this time. By 2005 the total VLT win in the Province stood at almost \$760.0 million, the highest win level achieved in the program.

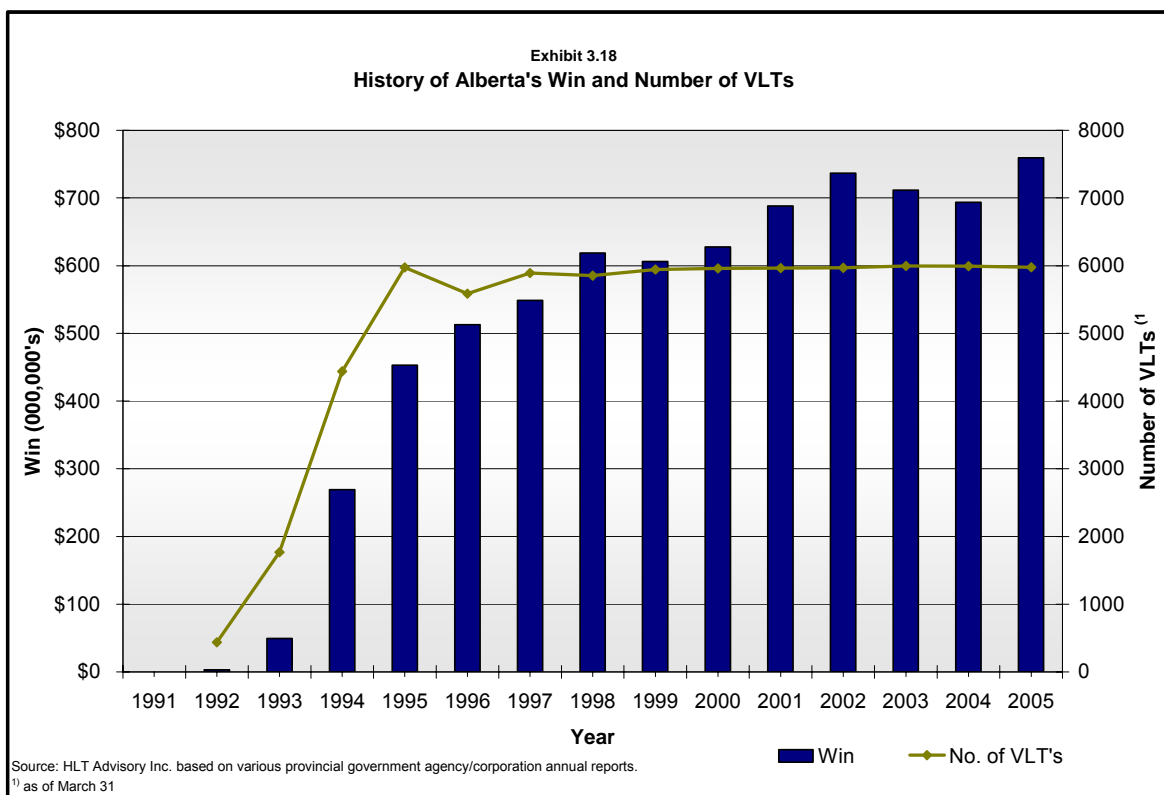


Exhibit 3.19
Saskatchewan Gaming Industry Win Trends by Sector

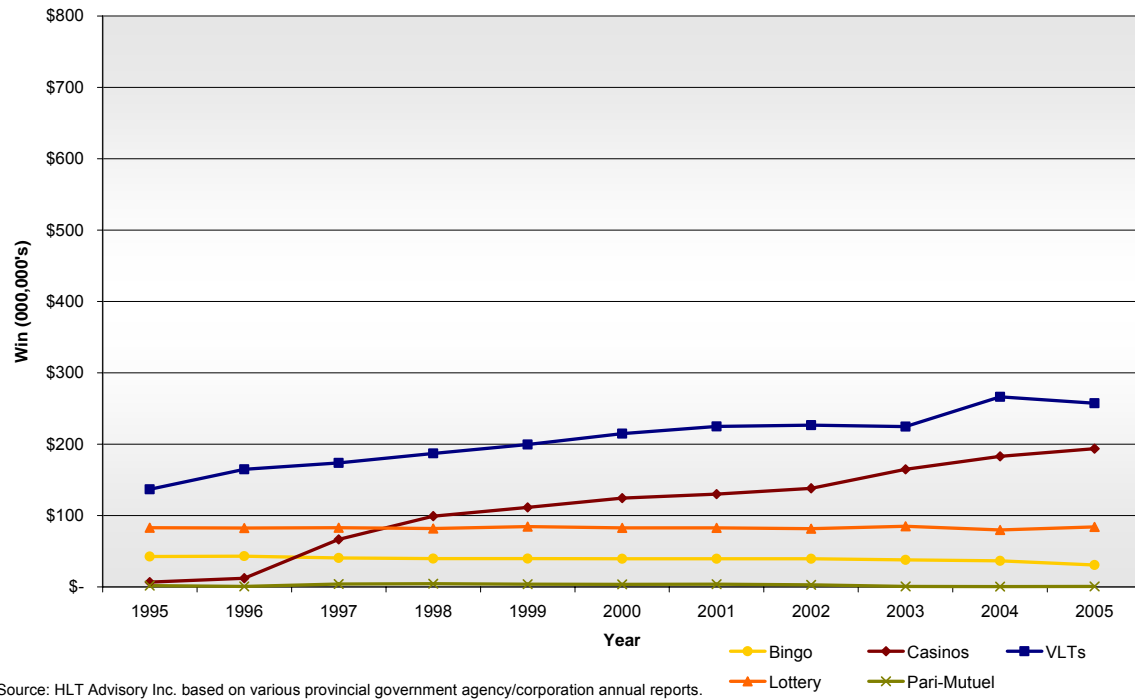
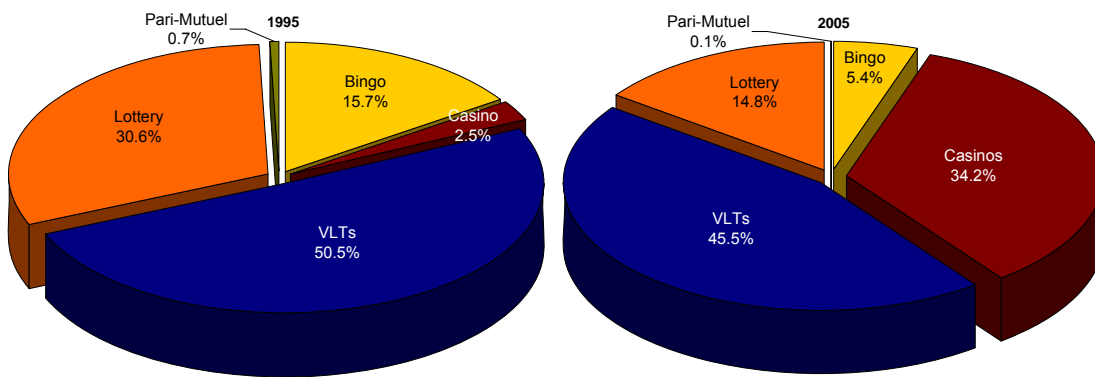


Exhibit 3.20
Saskatchewan Gaming Industry Win Share by Sector



3.7 SASKATCHEWAN

Saskatchewan's gaming industry has more than doubled in size from approximately \$271.0 million in 1995 to almost \$566.0 million in 2005. This \$300.0 million increase can be attributed almost entirely to casinos (approximately 60.0 percent) and VLTs (40.0 percent). Six casinos were constructed in Saskatchewan since 1995. By 2005, VLTs continued as the largest share of gaming revenue in Saskatchewan, accounting for 45.5 percent of the entire industry with casinos becoming the next largest sector at 34.2 percent (see Exhibits 3.19 and 3.20 facing).

Saskatchewan implemented a VLT program in July 1993 in response to concerns from the hospitality industry that local businesses, especially in rural communities, were losing business from residents travelling to neighbouring provinces to gamble. A major element of the program was to support rural communities by providing an additional form of entertainment for liquor licensed hotels and restaurants. VLTs were permitted only in those liquor licensed establishments that had a minimum seating capacity of 30, with 3 to 12 machines permitted per site. External advertising was not allowed and internal signage could only indicate that VLTs were onsite.

By 1995 the Province imposed a cap of 3,600 VLTs in the Province. Over the next seven years, the Province redistributed existing machines within the network in an attempt to balance consumer demand at all locations. By 2001 the Province initiated a program to replace the central server and individual machines. In 2002 the Province also increased the number of VLTs from 3,600 to 4,000.

Revenue from the VLTs was split, 85.0 percent to the Province and 15.0 percent to site holders. The Province was responsible for capital and operating costs. The Western Canada Lottery Corporation, of which Saskatchewan is a shareholder, operates the VLT system for Saskatchewan.

Responsible gaming initiatives were implemented in 2000, including training sessions for site holder personnel to increase understanding of both problem gambling issues and resources available to help problem gamblers. By 2002 the Province began to fund problem gambling prevention and treatment initiatives sponsored by Saskatchewan Health while continuing to provide training for site holder personnel. Upon replacement of VLT terminals, all new machines were fitted with certain responsible gaming features including:

- Cash display vs. credits showing the player's wager in actual dollars, not credits;
- Permanent on-screen clock reminding players of the actual time of day;
- Pop-up reminders at thirty minute intervals advising players how long they have been playing; and
- Enhanced banner display (problem gambling messages).

Exhibit 3.21 following illustrates the history of VLT gaming in Saskatchewan in terms of win and number of VLTs in operation. As shown, VLTs were implemented in the Province in a short period of time. Between 1995 and 2002 the number of machines was held constant just below the provincial cap of 3,600. The number of machines increased after 2002 due to the provincial cap being increased to 4,000. The number of sites has increased gradually from just over 500 in 1994 to almost 700 currently. Win generally increased steadily year over year to about \$260.0 million in 2005.

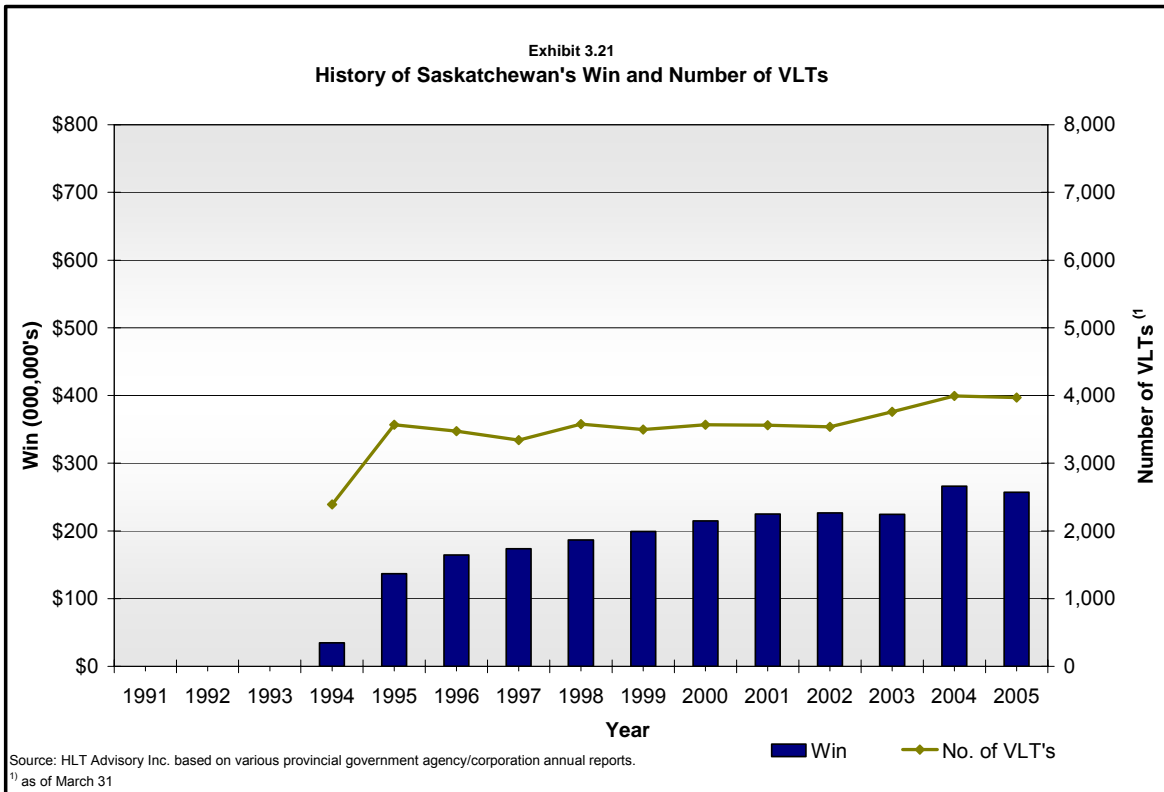


Exhibit 3.22
Québec Gaming Industry Win Trends by Sector

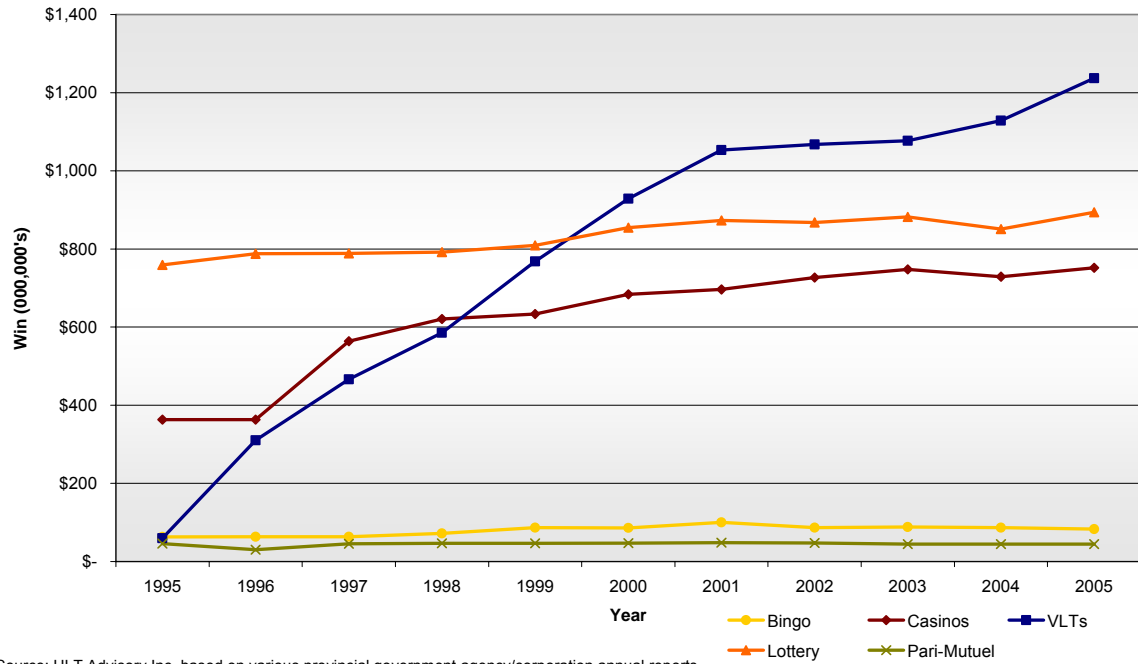
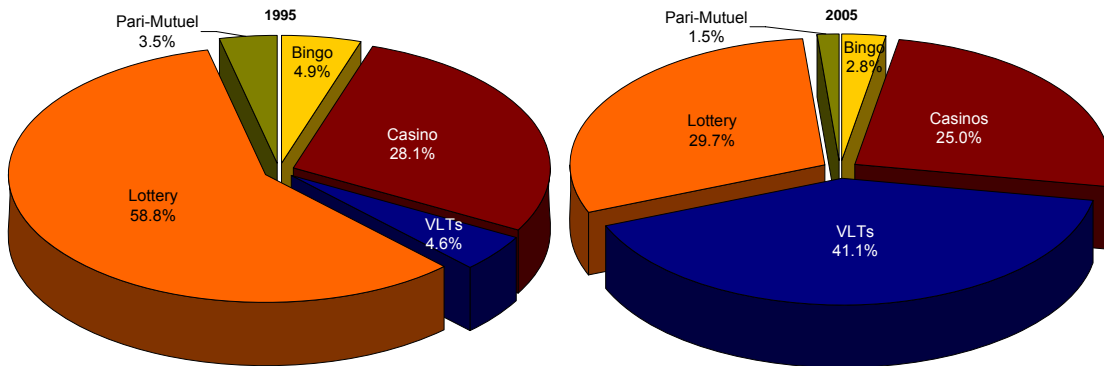


Exhibit 3.23
Québec Gaming Industry Win Share by Sector



3.8 QUÉBEC

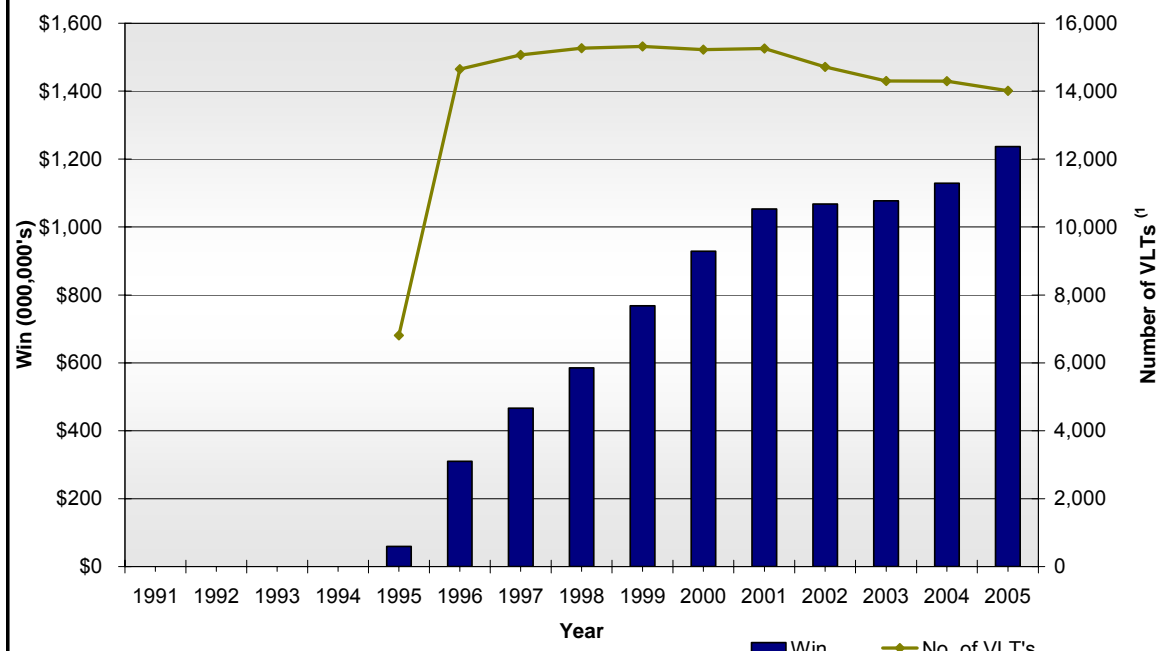
Québec's gaming industry more than doubled in size from approximately \$1.3 billion in 1995 to just over \$3.0 billion in 2004. Of this \$1.7 billion increase, VLTs accounted for more than \$1.1 billion, followed by casinos at almost \$400.0 million and lotteries at over \$100.0 million. In 1995 lotteries accounted for almost 60.0 percent of Québec's entire gaming industry. By 2005, due mainly to VLT and casino growth, lotteries declined to approximately 30.0 percent of the industry. VLTs increased its share of the industry from just below 5.0 percent in 1995 to over 40.0 percent in 2005 while casinos generally maintained its share (28.1 percent in 1995 and 25.0 percent in 2005 – see Exhibits 3.22 and 3.23 facing).

Québec initiated a VLT program in June 1994 allowing VLTs only in liquor licensed bars and brasseries. The main impetus for the program was to dismantle the network of some 40,000 illegal video poker machines that were reported to be in operation in the Province in 1993. These machines were both a large source of revenue for underworld groups and easily accessible to minors.

Between 1995 and 2000 the government fine-tuned the VLT system in terms of games, initiated responsible gaming measures across its entire gaming industry (including VLT sector) and undertook primary economic and social research into VLT gaming. In 2001 the government began planning for the replacement of all VLTs in the network and by 2003 the terminals were purchased and deployed. The new terminals were equipped with responsible gaming features such as:

- A permanent on-screen clock reminding players of the actual time of day;
- Players being required to indicate length of time they wish to play;
- Cash display vs. credits showing the player's wager in actual dollars, not credits;
- A module explaining the concept of chance integrated in the machines;
- Black surfaces as opposed to chrome on all machines;
- Warning messages about compulsive gambling;
- Problem gambling helpline visible on all machines;
- Maximum number of games on each machine reduced to five;
- Maximum wager decreased from \$100 to \$60;
- Playing speed reduced; and
- An automatic deactivation of units outside of authorized business hours.

Exhibit 3.24
History of Québec's Win and Number of VLTs



Source: HLT Advisory Inc. based on various provincial government agency/corporation annual reports.

⁽¹⁾ as of March 31

These machine features were combined with the implementation of a number of education measures aimed at increasing awareness of problem gambling. In addition, the advertising budget of VLTs was decreased by 10.0 percent and the number of machines was reduced from 15,300 to 14,300 in 2002. In 2004 the government offered financial incentives to site holders who withdrew fully or partially from the VLT program, resulting in 301 sites closing by the end of 2004. The commission rate paid to site holders was reduced from 26.0 percent to 22.0 percent of win. No new VLT sites have been introduced since 2001.

In 2005 the government further reduced the number of VLT sites by 31.0 percent, withdrew 2,500 VLT terminals from the network and reconfigured the VLT network to reduce game offerings in provincial sub-regions with “potential high social costs”. Of the 2,500 VLT terminals that were to be removed, 730 were to be permanently removed while the remaining 1,770 were to be relocated in a series of gaming centres around the Province. These new gaming centres would allow for more rigorous control to ensure compliance with regulations as well as better filtering of age restrictions and self-exclusion measures.

Exhibit 3.24 facing, illustrates the history of VLT gaming in Québec in terms of win and number of VLTs in operation. As shown, VLTs were implemented in the Province in a short period of time. Between 1995 and 2005 the number of machine increased to a high of 15,300 (1999), and subsequently reduced to 14,000 (2005). The number of sites peaked in 1997 at almost 4,400 and has been reduced to under 3,300 in 2005; these sites include four horse racetracks. The Province recently announced (2005) that three of these racetracks would receive additional VLT machines and the operations would essentially be transformed into “Racinos” with the VLT gaming component being operated by the government’s crown corporation responsible for gaming in the Province (Loto-Québec). Win increased steadily year over year since inception to about \$1.2 billion in 2005.

3.9 VLT GAMING IN THE UNITED STATES

Not including Nevada, six states offer VLT-style gaming similar to Canadian provinces. These states, along with the dates VLT gaming was implemented on, are:

- Montana (1985)
- South Dakota (1989)
- Oregon (1992)
- Louisiana (1992)
- New Mexico (1999)
- West Virginia (2001)

Montana and South Dakota implemented VLT-style gaming prior to any Canadian province. In fact, these two jurisdictions are cited by New Brunswick as examples used to develop its initial VLT program. In addition to these states, VLTs were operated in South Carolina throughout the 1990's, until being banned in July 2000.

Montana

Montana legalized video keno in 1976 and video poker in 1985. A state lottery was approved the following year. Today, there are some 1,700 VLT sites containing over 18,000 machines located throughout the state in liquor licensed facilities. These machines generated win of over \$350.0 million in 2005, of which the state received 15.0 percent as tax (the machines are owned by private sector operators). Since 1990 win has more than tripled while the number of machines in operation has almost doubled.

South Dakota

South Dakota passed video lottery legislation in 1989, pursuant to which VLTs were implemented that year, with regulatory responsibility under the state lottery. Operators own the terminals and contract with site holders to place machines in approved establishments and provide maintenance services. Three state-wide ballots to ban VLTs have been defeated since 1989. Additionally, in 1994 the state declared VLTs unconstitutional, which was subsequently reversed by a voter-approved constitutional amendment to reauthorize VLT gaming that same year.

In 1990 some 3,800 machines generated over \$46.0 million in win, which has increased year over year. Currently (2005) over \$220.0 million in win was generated by some 8,700 machines. These machines are currently located in 1,449 liquor licensed bars and lounges across the state. The state receives 50.0 percent of all win while the operators and site holders split the remaining amount.

Oregon

Oregon approved VLT legislation in 1991 and started installing machines the following year in age-controlled liquor licensed establishments. The impetus for this legislation was that the government estimated that up to 10,000 video slot and video poker machines ("grey" machines) were being used for illegal gaming in the state. Oregon Lottery regulates all VLT gaming and receives between approximately 75.0 and 80.0 percent of win (site holder commissions are based on a sliding scale of revenue and type of machine).

Oregon's VLT sector is very similar to the majority of Canadian provinces in that it is operated by a state lottery corporation and is a centrally controlled network with regulated location restrictions, wagering levels, prize payouts, average number of machines per site and revenue split. Currently some 2,041 sites containing almost 10,500 machines generate win of almost \$580.0 million. Win and the number of machines have increased year over year since inception. Oregon's VLT gaming sector is second only to Louisiana in the United States in terms of win.

Louisiana

In Louisiana electronic gaming devices are permitted to be installed in approved racetracks (and off-track betting facilities), truck stops, bars, restaurants and hotels. Only racetracks can apply for "slot machines" while all other locations are restricted to "video poker" machines. Video poker machines were legalized in Louisiana in 1991 and implemented in 1992, regulated by the state Gaming Control Board. The state tax on video poker machines (allocated to both state and local government) varies by site location with racetracks (and off-track betting facilities), truck stops and all other locations paying 22.5 percent, 32.5 percent and 26.0 percent respectively.

Currently there are some 14,270 video poker machines located in 2,750 non-racetrack locations throughout the state. All of these sites and machines are networked to a central hub controlled by the Gaming Control Board. These machines generated over \$580.0 million in win in 2005, making Louisiana's VLT gaming sector the largest in the United States. In 1999 the total video poker win in the state was over \$670.0 million (including racetracks). This level dropped to under \$480.0 million in 2000 as 33 of the state's 64 parishes voted to ban machines (the vote took place in 1996 and machines removed at the end of 1999).

New Mexico

New Mexico state legislation approved electronic gaming devices in 1997, implemented them in racetracks and certain non-profit organizations in 1999 with regulation by the New Mexico Gaming Control Board. The state tax on win from non-profit organizations is 10.0 percent (26.0 percent at racetracks). Currently there are only 605 machines in 59 non-profit locations throughout the state.

West Virginia

West Virginia implemented VLTs as a limited test at a single racetrack in 1990. Subsequent legislation allowed expansion to other racetracks in 1994. In 2001 VLTs were authorized for "adult environments" (Class A liquor license) and implemented in 2002, with the number of machines operating in these establishments (non-racetrack) limited to 9,000 state-wide. The state bill allowing VLTs also outlawed pre-existing "grey" or "poker" machines. While all machines are privately owned, they are networked and centrally controlled by the state. VLT retailers must:

- Ensure computer controller/validator unit is on at all times (and connected to the central control system);
- Install one or more security cameras and related equipment (equipment must operate twenty-four hours a day);
- Pay out all video lottery tickets printed by the machine within ten days;
- Post problem gambling warning messages; and
- Not advertise video lottery gaming (enacted in 2004).

The state receives between 30.0 and 50.0 percent of win from non-racetrack VLT revenue (based on a sliding scale calculated on a three-month daily revenue average) with site holders receiving the balance. Currently there are some 8,000 VLTs located in 1,658 non-racetrack locations. Win generated from these machines reached over \$310.0 million in 2005.

South Carolina

During the 1990's VLTs, commonly referred to as video poker machines, operated throughout South Carolina. Their operation was not initiated by design, but rather was the unforeseen consequence of a tiny amendment to a 1986 state budget bill combined with a state Supreme Court decision in 1991, which ruled that cash payouts from gaming devices were legal if the cash payout did not come directly from the gaming machine.

Prior to this court ruling, there were numerous video arcade-style games (video poker machines) in operation throughout the state. The ruling essentially allowed these machines to be instantly "turned into" gaming devices. South Carolina did not have a regulatory structure in place to administer this new form of gaming. There were no rules as to who could own and operate the machines and no operating standards. In fact, during the entire period that video poker operated, children could play the machines and individuals/businesses with criminal histories could own/operate machines. At various times throughout the 1990's the state attempted to create such a regulatory structure.

- In 1993 the state passed the *Video Game Machines Act*. This Act attempted to address hours of operation, the age of players to whom payouts could be made, residency of machine licensees, location of establishments and the number of machines allowed at a "single place or premise". The Act was immediately challenged in court, principally regarding the number of machines that were allowed at a single place or premise – the issue being the definition of a "single place or premise".
- In 1995 regulations dealing with the definition of a single place or premise, inducements to play, advertising and measurement of distance (proximity to schools and churches), were passed. However, the wording of the regulations did not prevent children from playing the gaming machines, but rather only prohibited them from collecting any winnings. Moreover, the state did not have the means to reliably monitor machine prize payout structures.
- In 1998 the state attempted to centrally monitor all VLT machines, by requiring all terminals to be hooked up to a state-controlled central system and to regulate the prize payouts, limiting payouts to \$125 per machine per day. Operators continued to offer large jackpots, circumventing the law by paying the larger jackpots out at a rate of \$125 per day until fully paid. As well, all machines were required to be certified to meet regulatory standards established by the state. In all cases, compliance was left to the private owners of the machines (a self regulated approach).

By the late 1990's some 34,000 machines were in operation throughout the state in 7,500 various types of establishments, such as convenience stores, pizza parlours, bowling alleys, bars, gas stations and "video game malls". A "video game mall" was simply a building that contained many separate rooms each containing a number of gaming machines. The entire building including all the rooms was operated by a single entity.

Finally, in 1999, the state renewed its attempt to regulate gaming activity through a series of new regulations, as well as enacting a law to hold a public referendum on whether or not residents wanted "video poker" gaming. The law stated that if a referendum was deemed unconstitutional, then all "video poker" gaming machines would be banned. In November 1999 the state Supreme Court ruled that a referendum was unconstitutional and as such, all "video poker" gaming machines were banned effective July 2000.

4. VLT Gaming Programs in Canada – Summary

This section of the report summarizes VLT gaming programs in Canada in terms of implementation rationale, regulations, responsible gaming, distribution models and economic models.

4.1 IMPLEMENTATION RATIONALE

Gaming in Canada has been implemented pursuant to certain stated government policy objectives. With respect to VLT gaming, two principle reasons or objectives most often cited are:

- To curb the growth of illegal gaming; and
- To support economic development initiatives.

These exact reasons or objectives were also cited in those states that implemented VLT gaming in the United States since 1990. Further, in Canada this time period corresponds with a shift in federal fiscal policy away from direct taxes and towards user fees. Also, provincial governments and sub-provincial governments were forced to provide services with less financial resources (reduced federal government transfer payments to the provinces). Gaming in general (including VLT gaming) represented a means to generate non-tax revenues to fund key government programs and initiatives in areas such as education and health.

Illegal Gaming

Four provinces (New Brunswick, Nova Scotia, Alberta, Québec) cite illegal gaming as a major reason for introducing legal VLT gaming. This circumstance is similar to that of a number of US jurisdictions that also implemented gaming in general and VLT gaming specifically. While the number of illegal VLT-type machines was difficult to substantiate in the early 1990's (as it is today), it was/is the assessment and repeatedly expressed judgment of Canadian law enforcement agencies that this type of illegal gaming exists and was more widespread prior to the introduction of regulated legal VLT gaming.

For instance, based on a review of readily available annual reports (1998 to 2005) of the Criminal Intelligence Service Canada ("CISC"), illegal gaming exists in every region of Canada. The forms of illegal gaming in Canada most often mentioned in these Annual Reports are VLT-type gaming, bookmaking and internet gaming. For example in its 1999 Annual Report, CISC states:

"Historically, illegal gaming has been the domain of organized crime. The threat of organized crime infiltration of legal gaming venues is ongoing.

The criminal element is well aware of the fact that illegal gaming offences are not an investigative priority in a number of provinces. There is little incentive to allocate scarce investigative resources to illegal gaming investigations, particularly where sentencing for non-violent crimes is minimal.

Casino loan sharking activity that targets compulsive or pathological gamblers creates additional risk. Gamblers who become indebted to these criminals may resort to crime to pay off debts and support their addiction.

Illegal gambling machines produce tremendous profits. Non-declared income from these machines is used by criminals to finance other criminal activities such as drug trafficking, money laundering and enterprise crime offences. Other gambling offences include illegal foreign and domestic lotteries, unauthorized pull-ticket distribution, bookmaking and illegal gaming houses.

There is no doubt that organized crime benefits from illegal gaming. In recognition of this, Criminal Intelligence Service Canada undertook a national illegal gaming initiative in 1998, in partnership with the Ontario Illegal Gaming Enforcement Unit.

The Ontario Illegal Gaming Enforcement Unit (OIGEU) comprises 40 investigators working in five regions of the Province. In 1998 the main challenges for OIGEU were video gambling machines, illegal gaming houses (card rooms) and bookmaking operations. Over the course of the year OIGEU seized 950 video gambling machines valued at approximately \$3 million. Gaming equipment from illegal card rooms was seized and cash confiscated from those operations. Four hundred and ninety-five people were charged with 787 gaming related offences. Those convicted paid over \$1 million in fines, forfeitures and surrendered proceeds of crime.

It is this type of proactive stance with regard to illegal gaming that Criminal Intelligence Service Canada hopes to promote with its national illegal gaming initiative."

Further, based on selected discussions with officials in the Canadian gaming industry (officials in the security and surveillance field of gaming) illegal gaming has never been a priority of major law enforcement agencies in Canada due to a lack of funding and priority focus on other crimes (i.e., violent crimes and drugs). With this said, a search of readily available Canadian law enforcement agencies' news releases and reports since the early 1990's uncovers many instances of illegal gaming machines having been seized and fines having been imposed.

Based on a review of secondary information sources in the United States as well as discussions with selected United States gaming industry officials, the Canadian experience outlined above is similar to the experience of many US jurisdictions. Illegal gaming still exists and it is not a priority focus of law enforcement officials. Selected states that currently are dealing with illegal gaming machines include Indiana, Maryland, North Carolina and Texas.

Given the lack of focus (due to a lack of funding and other priorities) that law enforcement agencies had paid to illegal gaming, certain provinces concluded that the introduction of legal VLT networks could help eliminate or at least curb the growth of illegal VLT gaming as well as illegal gaming in general. Operational issues related to illegal VLT gaming

included game integrity (ability to mechanically change machine payouts), participation of “underage” people and provision of credit (loan sharking).

Economic Development

In terms of economic development, the early 1990’s in Canada can be generally characterized as a period of economic recession and financial restraint. The focus of economic development initiatives at the federal and provincial levels in this time period was on assisting individual businesses through access to “grants” and low cost funding as opposed to “mega projects” which had characterized past government economic development policies.

Manitoba, Saskatchewan and Newfoundland and Labrador cited economic development initiatives as a major reason for implementing VLT programs. All three of these provinces have historically relied heavily on natural resources and/or farming as the backbones of their economies, and these industry sectors did not fare well in the early 1990’s. Their respective VLT programs allowed many small businesses located throughout these jurisdictions to receive financial assistance through site holder agreements (all provinces allocated a share of VLT win in lieu of rent to the owners of businesses where VLTs were located). In fact, many rural based hospitality businesses in these provinces avoided bankruptcy in the early 1990’s primarily due to VLT revenue.

The importance of VLT revenue to rural based hospitality businesses is still evident today. The Canadian Hotel Association issued an election platform (recent January 2006 Federal Election) that stated that “VLTs are an integral part of hospitality operations, particularly in rural hotels”. Further, the Association stated that it “would be opposed to any initiatives that would restrict VLTs to only casinos and racetracks”.

4.2 REGULATIONS

An important aspect of the operation of any gaming activity is the presence of clear operating rules and regulations. Rules and regulations protect the integrity of the gaming activity thus providing customers with the assurances that the games are fair and are conducted honestly. Equally as important as clear rules and regulations is the ability to enforce them. With regard to VLT gaming activity, key rules and regulations that are enforced relate to:

- Physical integrity of the machines
- Prize payouts
- Wagering limits
- Credit policies
- Prohibition of under-aged gaming

It is important to note here that all VLT machines in Canada are independently tested (hardware and software) before they are put into operation. Testing ensures that the machines will perform as intended, especially in regard to the rules and regulations governing the activity. Also, once the machines are operational, any changes to software or hardware are again tested to ensure the integrity of the activity.

Physical integrity of the Machines

Every province that operates a VLT program has networked the program whereby all machines in the network are connected (electronically) to a central control hub. This connection allows the operator (a provincial government crown corporation or agency) to monitor the activity of each individual machine, including ensuring that machines are not opened, that internal components are not tampered with and allowing for the continuous monitoring of cash in machines and payouts. If any terminal requires service, repair technicians can be centrally dispatched.

Prize Payouts

Prize payouts are an important component of the operation of any electronic gaming device. For VLT gaming activity in Canada, the prize payouts for each province are generally between 90.0 and 95.0 percent. This means that for every dollar that is wagered in a machine, between \$0.90 and \$0.95 is paid out as prizes (on average).

Wagering and Prize Limits

All VLT machines in Canada have wagering limit restrictions programmed into the terminals.

Credit

None of the VLT programs in Canada offer credit to patrons.

Prohibition of under-aged gaming

All VLT gaming in Canada (with limited specific exception) is permitted only in age-restricted liquor licensed establishments. This restriction does not apply to First Nations. In these instances the First Nation is required to impose physical measures to ensure that under aged people are not allowed access to the room or area that houses the VLTs. This type of operation requirement is stipulated in the various VLT agreements between provincial governments and individual First Nations.

4.3 RESPONSIBLE GAMING

As gaming has become both widely available and acceptable as a form of entertainment, people have become more aware of the potential for problem gambling. While individual personal responsibility and freedom of choice are primary to responsible gaming, the industry has studied the issue and developed a number of programs and safety features to assist people in this regard. This may be seen as analogous to the automotive industry, in that while the primary responsibility for safe driving does, and always will, rest with individual drivers, many secondary safety features are now (and are continuously being) built into passenger vehicles.

Broad key elements of all responsible gaming programs are:

- Education and awareness
- Prevention
- Treatment

The Canadian gaming industry is at the forefront of responsible gaming strategy programs. Based on the most recent *Canadian Gambling Digest* (2003-2004 report prepared by the Canadian Partnership for Responsible Gambling), Canadian provinces currently spend approximately \$62.0 million on problem gambling treatment, research and awareness prevention initiatives. In addition, over \$13.0 million is spent in the area of responsible gambling initiatives.

Specific to VLT gaming, all provinces offering this form of gaming have developed and implemented responsible gaming programs that include both general messages and specific features installed on the VLT terminals themselves. Exhibit 4.1 following summarizes these machines and program features.

Exhibit 4.1 Responsible Gaming VLT Program and Machine Features								
VLT Machine Features	Alberta	Sask.	Manitoba	Quebec	NS	NB	PEI	Nfld.
Permanent on-screen clock (Actual Time)	√	√	√	√**	√	√	√	√
Amount wagered displayed in dollars	√	√	√	√	√	√	√	√
Pop-up reminders to display time played on machine	√	√	√	√	√	√	√	√
Mandatory Cashout	√	√	√	√	√	√	√	√
Problem Gambling Help line number prominently displayed	√	√	√	√	√	√	√	√
VLT Program Features								
Responsible gaming posters, messages and brochures displayed at VLT sites	√	√	√	√	√	√	√	√
Restricted access and view of VLTs	√	√	√	√	√	√	√	√
Restrictions on VLT advertising	√	√	√	√	√	√	√	√
Staff training programmes to recognize problem gambling signs	√	√	√	√	√	√	√	√

Source: HLT based on reviews of provincial gaming agencies' websites and published reports.
 Note: In Quebec, players choose the time spent on the VLT in advance.

As shown, the majority of provinces have adopted and installed a number of similar machine and program features. Further, provinces such as Nova Scotia and Alberta have initiated research programs to test the effectiveness of these machine and program features. An important aspect of these research programs is the ability to measure these programs over time so as to efficiently and effectively make adjustments based on survey results of VLT participants.

4.4 DISTRIBUTION MODELS

All provincial VLT programs follow a general distribution model based on population distribution throughout their respective jurisdictions. This model provides all residents with a similar degree of opportunity or accessibility to game if they so choose. With regard to combating illegal gaming, this distribution model also ensures that all residents have access to a legal form of gaming and as such an alternative to illegal gaming. The distribution model is also consistent with the cited economic development initiative of certain provinces, which focuses on direct financial assistance to local hospitality businesses. The VLT gaming distribution model is also virtually the same as the lottery gaming model used by all provinces in Canada except for the restriction limiting installation to age-controlled liquor licensed establishments.

4.5 ECONOMIC MODELS

There is a general overall standard economic model for VLT programs in Canada.

- All are operated by a provincial government controlled crown corporation and/or agency.
- The province retains the majority of revenue (70.0 to 85.0 percent of win) while site holders (individual business owners that “rent space” for machines in their establishments) receive a small share (15.0 to 30.0 percent of win).
- All provinces cover capital and virtually all operating costs of the VLT machines.
- All provinces direct part of their share of revenue (after capital and operating costs) towards general provincial revenue funds and/or specific programs or areas (i.e., health, education, etc.).

Since 1991 VLT gaming in Canada has generated over \$25.0 billion in win. Provincial governments have generally received (before capital and operation costs) approximately \$18.0 to \$19.0 billion of this total. Site holders have received approximately \$6.0 to \$7.0 billion. *Note: Initially private sector operators did participate in the operation of New Brunswick's and Prince Edward Island's VLT program. Private sector operators were phased out in these two provinces due in part to interpretations of those sections of the Canadian Criminal Code that pertain to the operation of electronic gaming devices (only a province can offer games of chance played through an electronic gaming device).*

This economic model differs from the general model that exists in the six US jurisdictions that have VLT programs in that five of the six states' private operators and site holders retain the majority of VLT win while the state government receives a smaller percentage share (up to 50.0 percent) of win (Oregon being the sole exception with the state lottery owning the machines and operating the network, similar to Canadian VLT programs). In cases where there are private sector operators, the operators own the machines and are responsible for both the purchase and maintenance of the VLTs.

4.6 CONCLUSIONS

Since 1990 all provinces in Canada further developed their individual gaming industries in response to growing market demand and product maturation. The most significant developments were the introduction of VLT gaming, casinos and other EGD facilities ("racinos").

- Eight provinces in Canada operate VLT programs in their respective jurisdictions. Six implemented their programs in either 1991 or 1992 while the remaining two were implemented in 1994 and 1995.

VLT gaming programs in Canada have been built upon certain principles (economic development, combating illegal activities and generating non-tax government revenues), sound rules and regulations and consistent distribution and economic models. These programs have not been static. Rather, they have been developed and modified to address changing circumstances, including market demand, improvements in technologies, research and public opinion, such as:

- VLT machines are now restricted to age-controlled establishments
 - Today, all provinces only allow VLT gaming in age-controlled liquor licensed establishments with a single exception being that First Nation VLT gaming is generally exempt from this location/site requirement. Three provinces did initially allow machines to be installed in non-liquor licensed establishments but later reversed this policy decision (Nova Scotia in 1993, Prince Edward Island in 1998 and New Brunswick in 1999). These provinces were three of the first to introduce VLT gaming in 1991 and 1992.
- The number of machines and/or sites are periodically reviewed and/or adjusted.
 - Once implemented, all provinces have capped the number of VLT machines permitted in their respective jurisdictions and/or reduced the number of machines in operation (including recent planned reductions yet to be implemented) and/or reduced the number of sites offering VLT gaming (including recent planned reductions yet to be implemented).
- Responsible gaming features have been and will continue to be implemented.
 - A general trend in the late 1990's in the entire Canadian gaming industry (as well as in North America as a whole) has been the further enhancement of responsible gaming programs and measures. Canada is considered to be at the forefront of responsible gaming initiatives in terms of both funding and the continued enhancements and program developments. All provinces in Canada have adopted responsible gaming programs and measures covering their entire gaming industry.

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- Specific to VLT gaming, measures include physical machine features dealing with education and awareness. Many of these physical features were not readily available when VLT machines were first purchased and implemented. When these initial machines were replaced, all new machines included certain of these features. Most provinces have replaced their initial VLT machines since 2000.

VLT gaming, when compared to casino and other forms of gaming, is a more cost efficient gaming model from both the capital cost and operating perspectives, especially in relation to serving smaller more dispersed populations. Casinos, in particular smaller casinos, have a greater amount of fixed operating costs proportionately than do VLT programs. Moreover, these operating costs do not fluctuate with changes in business volumes. VLTs can be located in areas where the population base does not support the development and operation of a casino.

While the number of illegal VLT-type machines is difficult to substantiate, it is the assessment and repeatedly expressed judgement of Canadian law enforcement agencies that this type of illegal gaming exists, and was more widespread prior to the introduction of regulated legal VLT gaming.

Those opposed to gaming often cite the experience in South Carolina as typical of VLT gaming in Canada. This comparison is unfounded. Video poker was operated in South Carolina in an uncontrolled and unregulated environment, by individuals and organizations not subject to any licensing, scrutiny or oversight. There was no effective regulation preventing children from playing the machines and individuals/businesses with criminal histories from owning/operating them.

South Carolina provides a clear and compelling example of not only the need for clear rules and regulations, but also for the enforcement of such. In summary, legislators and law enforcement played "catch up" from the start. South Carolina did not initially approve of this style of gaming, but more significantly, it also did not stop the gaming activity pending proper decisions being made regarding ownership and operating models, taxation, regulation and enforcement. Rather, South Carolina inadvertently sanctioned the activity and then followed with repeated ineffectual attempts to establish rules and regulations and to impose a regulatory structure. The South Carolina experience stands in stark contrast with the current reasoned and well thought out pro-active approaches and programs operating in Canada.

In summary, VLT gaming in Canada:

- Is well regulated by Crown agencies;
- Is honestly and transparently operated by Crown agencies;
- Offers fair games in safe, age and access-controlled environments; and
- Raises significant non-tax revenues to fund key government programs and initiatives.

APPENDIX A BIBLIOGRAPHY

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